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THE BUDGETARY STATUS OF THE FEDERAL RESERVE SYSTEM

HEARINGS

BEFORE THE

SUBCOMMITTEE ON ECONOMIC GOALS AND
INTERGOVERNMENTAL POLICY

OF THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

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CONTENTS

WITNESSES AND STATEMENTS

TUESDAY, MAY 21, 1985

Page
Hamilton, Hon. Lee H., chairman of the Subcommittee on Economic Goals and Intergovernmental Policy: Opening statement 1
Penner, Hon. Rudolph G., Director, Congressional Budget Office 2

THURSDAY, JUNE 27, 1985

Hamilton, Hon. Lee H., chairman of the Subcommittee on Economic Goals and Intergovernmental Policy: Opening statement 143
Volcker, Hon. Paul A., Chairman, Board of Governors, Federal Reserve System 147

SUBMISSIONS FOR THE RECORD

TUESDAY, MAY 21, 1985

Penner, Hon. Rudolph G.: Report entitled "The Budgetary Status of the Federal Reserve System," by the Congressional Budget Office 7

THURSDAY, JUNE 27, 1985

Hamilton, Hon. Lee H.:
  Text of H.R. 1659, a bill to amend section 1105 of title 31, United States Code, relating to the President's budget to require it to separately set forth the annual budget of the Federal Reserve System 145
  Annual report of the Federal Reserve Bank of Cleveland for 1984 314
Volcker, Hon. Paul A.: Prepared statement, together with attached appendixes 152

J 841-5

THE BUDGETARY STATUS OF THE FEDERAL RESERVE SYSTEM

TUESDAY, MAY 21, 1985

Congress of the United States,
Subcommittee on Economic Goals
and Intergovernmental Policy
of the Joint Economic Committee,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:05 a.m., in room 2337, Rayburn House Office Building, Hon. Lee H. Hamilton (chairman of the subcommittee) presiding.

Present: Representatives Hamilton and Snowe; and Senator D'Amato.

Also present: William R. Buechner, Joe Cobb, and Kent Hughes, professional staff members.

OPENING STATEMENT OF REPRESENTATIVE HAMILTON, CHAIRMAN

Representative Hamilton. The subcommittee will come to order.

We are pleased to welcome Mr. Rudolph Penner, Director of the Congressional Budget Office, to testify today on the treatment of the budget of the Federal Reserve System.

In a democracy it is essential that the citizens and voters have access to how the Government spends the taxpayers' money. The source of that information is the annual budget of the United States Government which not only includes broad spending totals by function and agency, but also in the appendix gives the details on each agency's spending.

Armed with this information, voters can judge how well the Government is carrying out its responsibilities.

There is one major Government agency, however, whose spending is not in the budget, and that is the Federal Reserve System. Although the Fed has justified this exclusion in various ways, first by arguing that it is private because its stock is owned by the member banks and, more recently, by arguing that losing control over its budget would reduce its independence in monetary policy matters, the same rule should apply to the Fed as applies to other Government agencies: No agency of the Government should be able to take in and spend billions of dollars without having its budget open to public view.

I recognize that the Federal Reserve has special responsibilities that may require it to take actions that are unpopular, but the Fed's need for a measure of independence from political pressure is no excuse for shielding its budget from some process of accounting to Congress and the public.

In 1983, the most recent year for which we have figures, the Federal Reserve System had revenues of just over $16 billion. Most of this came from interest paid by the Treasury on the Fed's portfolio of U.S. Government securities. The Fed used about $1.75 billion of this to meet its operating expenditures and other obligations, and returned just over $14.2 billion to the Treasury where it was used to reduce the deficit. The only part of this to appear in the budget is the amount returned to the Treasury which is included under the heading, "Miscellaneous Receipts."

Recently, I introduced legislation to have the Federal Reserve publish its annual budget as part of the budget of the United States Government. The bill would put the revenues and expenditures of the Board of Governors and all the Federal Reserve Banks into the Federal budget beginning in fiscal year 1987. Figures would have to be presented in a format consistent with the budget data for other Government agencies, and projections would have to be made in each budget for the two subsequent fiscal years as well.

The Fed would still have full control of its budget, but the Congress and the public would have the information.

In February, the Congressional Budget Office completed a major study of the Federal Reserve's budget status for the Joint Economic Committee. We will now turn to Mr. Penner's testimony on the findings and conclusions of that study. Paul Volcker, Chairman of the Board of Governors of the Federal Reserve, will testify on the same subject at a hearing scheduled for next month.

Mr. Penner, we have your statement. It will, of course, be entered into the record in full. You may read it or summarize it, as you choose. We appreciate your coming before the subcommittee this morning and we look forward to your testimony.

STATEMENT OF HON. RUDOLPH G. PENNER, DIRECTOR, CONGRESSIONAL BUDGET OFFICE

Mr. **Penner**. Thank you very much, Mr. Chairman. I am pleased to testify before this subcommittee on the proposal to include a presentation of the Federal Reserve System's finances in the unified budget of the United States. The Congressional Budget Office, CBO, has prepared a report on the budgetary status of the Federal Reserve, as you said. That report has been distributed to members, and I hope that it can be included in the record.

Representative **Hamilton**. Without objection, the report will be included in the record in its entirety.

Mr. **Penner**. In my remarks today, I will describe the current budgetary treatment of the Federal Reserve System to indicate why a more complete presentation of the System's finances would be useful. I will also note some difficult issues that would be raised by including all activities of the Federal Reserve System in the unified budget.

CURRENT TREATMENT

The current budgetary presentation of the Federal Reserve's finances is incomplete compared with that of other independent Government agencies. The main budget document includes an entry for Federal Reserve net earnings transferred to the Treasury. For 1985, these "miscellaneous receipts"—as they are called—from the deposit of Federal Reserve earnings are expected to total $18 billion. The Federal Reserve earnings consist of gross income minus operating expenses, dividend payments to member banks, and other adjustments. Gross income and expenses are not shown separately in the budget.

The Budget Appendix, but not the main budget document, reports operating expenses for the Board of Governors. Reserve Bank expenses—accounting for about 95 percent of the system's expenses—are not shown. Further, the expenses of the Board of Governors are reported only for the current calendar year rather than for the projected fiscal year. To the extent that the System's accounts are available to the public, they are generally not comparable with budget data. For example, purchases of capital goods are handled in the Federal Reserve accounts more as they would be in a private firm rather than on the cash-flow basis used in the budget.

THE CASE FOR A MORE COMPLETE AND CONSISTENT BUDGET STATEMENT

On its face, the current budgetary treatment of the Federal Reserve violates a basic principle of budgeting; namely, that the budget document should be comprehensive about Government operations and should facilitate cost comparisons among agencies and activities. More particularly, the reporting of net earnings provides little information about financial performance or operating characteristics of an agency with the power to create money. Although the distinction between the expenses of the Reserve Banks and the Board of Governors may once have had some justification in the technical status of the banks as "privately owned," it is now clear that the Federal Reserve's earnings accrue to the Treasury; thus, when a Reserve Bank spends money for a new building or check processing center, public moneys are being dispensed. Finally, the continued adherence by the Board to a calendar-year budget statement confuses attempts to compare their accounts with the fiscal-year accounts of other agencies.

This failure to explicitly show the expenses of the Federal Reserve leads to underreporting of Government outlays for financial regulation, economic policy, and Government financial services. The large volume of Federal Reserve business-type activities—check collection and the electronic transfer of funds, for example—are obscured from public view.

It is tempting to conclude, therefore, that the Federal Reserve System should be brought fully on-budget and afforded the same fiscal accounting treatment as the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the Federal judiciary, for example. Nonetheless, an attempt to increase the comprehensiveness and content of the unified budget by including a complete statement of Federal Reserve activity would raise difficult policy and accounting questions that need to be addressed.

SPECIAL DIFFICULTIES RAISED BY THE BUDGETARY TREATMENT OF A CENTRAL BANK

Most of the troublesome issues involved in putting the Federal Reserve fully on-budget arise because of the System's role as the Nation's central bank. In this section of my testimony, I will focus on several of these issues by considering three budgetary treatment options for the Federal Reserve: first, adding only the Reserve System's operating costs to the budget; second, including the financial transactions along with operating expenses; and third, appropriating funds for Reserve System operations.

DISPLAYING OPERATING EXPENSES

A long-standing, but not unquestioned, American political tradition suggests that in order to discharge its responsibilities for maintaining a sound currency and for avoiding financial crises, a central bank must have a degree of policy independence from both the executive and legislative branches of Government. My understanding is that the proposal being considered here is not intended to modify the existing balance of authority over monetary policy. Rather than mandate prior congressional approval of the System's budget, which might be interpreted as a means to exert detailed influence over monetary policy, the intent is simply to require the Federal Reserve to account for its operating expenses in the same terms as other federal entities. Some conflict exists, however, between the basic purpose of the budget and its use merely as a means for promoting disclosure.

Comprehensiveness is desired in a budget precisely to ensure that all resources are subject to the allocative decision process. No agency or use is presumed to have a first claim on fiscal resources. But in the case being considered here, the intent is to include expenditures in the budget without exercising any control over their use. Although this is at odds with the basic concept of allocative budgeting, it would not be the only example of this phenomenon found in the budget. Trust funds and revolving funds, for example, are now on-budget, even though the moneys they receive are not routinely considered for reallocation to other uses.

The urgency of the case for including operating expenses in the budget is dampened somewhat by the legislated requirement that the Federal Reserve compete fairly in the market for financial services by charging full-cost prices for many of its services and by the reimbursement it receives for costs incurred on behalf of other Government agencies. Over 55 percent of Federal Reserve expenses for services to agencies and private financial institutions is now recovered from beneficiaries. Putting these accounts on-budget, therefore, would consist largely of adding both outlays and their offsetting receipts.

INCLUDING FINANCIAL TRANSACTIONS

Most of the Federal Reserve disbursements are to acquire financial assets, specifically to purchase U.S. Government securities and to make loans to financial institutions. In fact, these disbursements dwarf operating costs. Completeness of budgetary coverage would require that these transactions be included in the budget even though they are usually offset within days by the sale of assets and by the repayment of Reserve Bank advances.

Under current budget practice, these financial transactions would be reported on an annual, net assets acquired basis. This netting process will mask an enormous amount of activity and, simultaneously, fail to capture the value of subsidies that may be conveyed through discount window loans.

The Federal Reserve is not unique among Government agencies as a dealer in financial assets and provider of credit assistance. The Export-Import Bank of the United States and the Federal Deposit Insurance Corporation, for example, are engaged in acquiring and managing substantial quantities of financial assets. Both institutions are on-budget even though Federal budget accounting is not well suited to their operations. For example, net lending during the fiscal year, which is what is shown in the budget, tells us little about the value of the subsidy inherent in the lending.[1] The imperfections of the current budget system, however, have not been regarded as a sufficient reason for omitting an activity or agency from the budget.

Another aspect of the issue of policy independence is raised by the need to project future data for budget accounts. In the case of the Federal Reserve, projections of asset holdings may be interpreted as an announcement of or a target for future monetary policy. One way to avoid such an interpretation would be to adopt as a budget convention the practice of extrapolating Federal Reserve accounts solely on the basis of current policy. Such a projection would provide the budget with "order of magnitude" numbers but would not commit the Federal Reserve to a particular policy course.

APPROPRIATING FEDERAL RESERVE EXPENDITURES

Alternatively, as noted in the CBO report, Federal Reserve operating expenses would be explicitly subject to congressional appropriation. While this approach may suggest an increase of congressional influence over monetary policy, that suggestion might be minimized by restricting coverage of budget and appropriations to functional expenses other than those incurred in the design and execution of monetary policy. The separation of monetary policy expenses from all other expenses, however, will not be easily accomplished because of shared support and overhead cost. A danger exists also that legislative riders would be attached to such appropriations and used to influence monetary policy.

SUMMING UP

The current budget presentation for the Federal Reserve is incomplete, inconsistent with many other accounts, and less useful than the budget statements for many independent agencies. These deficiencies go beyond what can be justified by a desire for an independence of monetary policy or the special nature of central banks. But it is not completely clear that the best solution would be to bring the Federal Reserve immediately and fully on-budget. The limitations of the current budget accounting system are a concern. Moreover, it must be noted that accounting and budgetary changes of this magnitude increase accounting costs by nontrivial amounts. But the major unresolved issue is the extent to which a budgetary change would reduce to an undesired extent the Federal Reserve's policy of independence.

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[1] For a detailed discussion of the failings of the budget treatment of Federal credit, see Congressional Budget Office, "New Approaches to the Budgetary Treatment of Federal Credit Assistance" (March 1984).

The risk is greatest if Federal Reserve expenses are appropriated and if the Federal Reserve is required to project its annual financial operations. The risk is smaller if the budgetary coverage is primarily informational and limited to operating expenses. The expected gain from taking these risks would be to provide better information for congressional oversight. This is not an easy choice, nor is it one that the CBO is equipped to make. I think it is, rather, a matter for congressional judgment. Thank you very much, Mr. Chairman.

[The report referred to for the hearing record follows:]

7

THE BUDGETARY STATUS OF THE FEDERAL RESERVE SYSTEM

The Congress of the United States
Congressional Budget Office

PREFACE

This report on the budgetary status of the Federal Reserve System was undertaken at the request of the Joint Economic Committee. The study describes the structure, activities, and financing of the Federal Reserve System, and reviews the history of the budgetary independence of the System. It considers in detail two proposed alterations in the Federal Reserve's budgetary status: a complete presentation of Federal Reserve System finances in the budget, and a requirement of prior appropriations for Federal Reserve System expenditures. The study does not examine in detail the Federal Reserve's determination and conduct of monetary policy.

The study was prepared by Roy T. Meyers of the Budget Process Unit under the supervision of Richard P. Emery, Jr. David Delquadro, Mitchell Mutnick, and Marvin Phaup contributed material and valuable advice. Useful comments and suggestions were made by Valerie Amerkhail, Jacob Dreyer, Louis Fisher, Robert Hartman, Mary Maginniss, Marty Regalia, Stephen Swaim, Jean Wells, and John Woolley. Francis S. Pierce edited the manuscript. Paula Gatens prepared the manuscript for publication.

Rudolph G. Penner
Director

February 1985

CONTENTS

PREFACE iii

SUMMARY xi

CHAPTER I. INTRODUCTION 1

CHAPTER II. A HISTORY OF THE BUDGETARY INDEPENDENCE OF THE FEDERAL RESERVE SYSTEM 3

The Federal Reserve Act 3
The Banking Acts of the 1930s 7
The "Accord" 8
The Martin-Patman Years 10
The Recent Decade 12
Summary 14

CHAPTER III. AN OVERVIEW OF THE FEDERAL RESERVE SYSTEM 19

Structure 19
Activities 20
Financing and Expenditures 26

CHAPTER IV. BUDGET PRESENTATION 39

Limitations of the Current Budget Presentation 40
Reasons for the Current Budget Presentation 44
Federal Reserve Finances and Current Budget Concepts 49
Predictability as a Factor 56
The Federal Reserve's Independence 59
The Mechanics of Budget Presentation 60

CONTENTS (Continued)

CHAPTER V. THE FEDERAL RESERVE SYSTEM AND THE APPROPRIATIONS PROCESS 63

- Congressional Spending Control Processes 64
- Alternative Methods of Evaluating the Spending Record of the Federal Reserve 71
- Federal Reserve Budget Savings Approaches 86
- The Appropriations Process and Congressional Policy Direction 94

APPENDIX A. BUDGET PRESENTATION COMPARISONS 97

APPENDIX B. BUDGETING IN THE FEDERAL RESERVE SYSTEM 105

TABLES

TABLE 1. INCOME, EXPENSES, AND EARNINGS OF THE FEDERAL RESERVE BANKS, 1983 28

TABLE 2. STATEMENT OF CONDITION, FEDERAL RESERVE BANKS, 1983 29

TABLE 3. FEDERAL RESERVE BANKS' CAPITAL OUTLAYS, 1983 31

TABLE 4. FEDERAL RESERVE BANKS' TOTAL OUTLAYS, 1983 32

TABLE 5. COMPOSITION OF FEDERAL RESERVE BANKS' CURRENT DIRECT AND INDIRECT EXPENSES, 1983 33

TABLE 6. COMPOSITION OF FEDERAL RESERVE BANKS' CURRENT EXPENSES, NET OF REIMBURSEMENTS AND COLLECTIONS, 1983 34

TABLE 7. INCOME AND EXPENSES OF THE BOARD OF GOVERNORS, 1983 35

TABLE 8. COMPOSITION OF BOARD OF GOVERNORS' EXPENSES, 1983 36

TABLE 9. FEDERAL RESERVE BUDGET PRESENTATION FOR FISCAL YEAR 1985: TOTAL BUDGET RECEIPTS 42

TABLE 10. FEDERAL RESERVE BUDGET PRESENTATION FOR FISCAL YEAR 1985: BUDGET APPENDIX PROGRAM AND FINANCING SCHEDULE 43

TABLE 11. THE UNIFIED BUDGET OUTCOMES OF FEDERAL RESERVE INCOME RECLASSIFICATION AND EXPENSE PRESENTATION 57

TABLES (Continued)

TABLE 12. FEDERAL RESERVE EARNINGS TRANSFERS AND NET BUDGETARY INTEREST 58

TABLE 13. TOTAL FEDERAL RESERVE SYSTEM EXPENSES, CALENDAR YEARS 1979-1983 72

TABLE 14. SELECTED ECONOMIC STATISTICS AND POLICY EXPENSES, FISCAL YEARS 1979 AND 1983 73

TABLE 15. ADMINISTRATIVE EXPENSES OF FEDERAL AGENCIES WITH FINANCIAL REGULATION DUTIES, FISCAL YEARS 1979-1983 74

TABLE 16. COMPOSITION OF FEDERAL RESERVE BANKS' CURRENT EXPENSES, 1979-1983 75

TABLE 17. COMPOSITION OF BOARD OF GOVERNORS PROGRAM OBLIGATIONS, 1979-1983 76

TABLE 18. FEDERAL RESERVE BANKS: PRICED SERVICES EXPENSES AND REVENUE, 1983 83

TABLE A-1. OFF-BUDGET FEDERAL ENTITIES AND GOVERNMENT-SPONSORED ENTERPRISES, FISCAL YEAR 1985 98

TABLE A-2. CHARACTERISTICS OF ORGANIZATIONS WITH ACTIVITIES SIMILAR TO THOSE OF THE FEDERAL RESERVE SYSTEM 100

BOXES

FEDERAL RESERVE FINANCIAL OPERATIONS 41

BUDGET TREATMENT OF THE CONTINENTAL ILLINOIS DISCOUNT LOAN 54

SUMMARY

The Federal Reserve System was established by the Federal Reserve Act of 1913 to serve as the nation's central bank. Underlying its creation was the desire for an efficient payments system and an elastic currency. To accomplish these purposes, the Federal Reserve Banks were granted the powers to transfer funds nationwide and to advance funds to member banks. The Banks were also given the duties of issuing currency and handling government deposits and debt issues. These responsibilities have since expanded, and the System currently provides many services to the financial sector and the government.

As the Federal Reserve System matured, two additional responsibilities--the determination and conduct of monetary policy and the supervision and regulation of part of the banking system--became more important. Monetary policy is considered to be its most important activity. The Federal Reserve attempts to promote price level stability and high levels of production and employment by influencing the quantity of money and the price of credit (interest rates). Its primary policy instrument is the purchase and sale of government securities in the open market. In concert with the Treasury, the Federal Reserve also trades in currencies to moderate movements in the foreign exchange value of the dollar.

The Federal Reserve shares responsibility for supervision and regulation of the commercial banking sector with the Comptroller of the Currency and the Federal Deposit Insurance Corporation. It is primarily responsible for the regulation and supervision of bank holding companies and state chartered banks that are members of the Federal Reserve System. The System also writes regulations for consumer protection and credit availability laws.

THE FEDERAL RESERVE'S STRUCTURE AND FINANCES

The structure of the Federal Reserve System has remained relatively unchanged since passage of the Federal Reserve Act. The Board of Governors in Washington sets general operating policies for the System as a whole. The Board is composed of seven members appointed by the President and confirmed by the Senate, and is assisted by a staff of about 1,600 persons.

Most of the operations of the System are carried out by 12 Federal Reserve Banks and their branches and other facilities located throughout the country. Each Bank has nine directors, six selected by member banks and three appointed by the Board of Governors, two of whom serve as chairman and deputy chairman. The directors appoint the chief operating officers of the Banks with the approval of the Board of Governors. The Federal Reserve Banks have about 23,000 employees.

The Federal Open Market Committee, which meets in Washington at frequent intervals, is responsible for determining the course of monetary policy. The Committee consists of the seven Governors of the Board and five Reserve Bank Presidents. The Federal Reserve Bank of New York carries out the Committee's directives. Nearly 6,000 commercial banks are "member banks" of the System.

The Federal Reserve Banks earn almost all of the income of the Federal Reserve System, and spend approximately 95 percent of its gross expenses. Income exceeded $16 billion in calendar year 1983, 94 percent of which was interest earnings on U.S. government securities. Operating expenses of the Federal Reserve Banks were about $1.1 billion dollars in 1983. The Board of Governors spent about $70 million with funding from assessments on the Federal Reserve Banks.

In 1983, nearly $700 million of the System's gross operating expenses were for providing services to financial institutions and the public, and nearly $500 million was received in compensation for these services. Expenses for supervision and regulation of banks were nearly $150 million, and expenses for economic policy exceeded $100 million. Gross expenses for services to government agencies exceeded $120 million, and the agencies reimbursed 60 percent of these expenses.

THE FEDERAL RESERVE'S BUDGETARY STATUS

The budget of the Board of Governors for the most recent calendar year is printed in the Budget Appendix along with those of other off-budget entities such as the Federal Financing Bank, the Postal Service, and the U.S. Synthetic Fuels Corporation. The Board's expenses are not included in the budget's tabulation of total off-budget outlays, however, and because the Board's budget is presented on a calendar year basis it does not cover most of the federal budget year.

The financial operations of the Federal Reserve Banks are not shown in the federal budget documents. They are instead reported to the Congress in the Annual Report of the Board of Governors. The report is limited to the completed calendar year, and does not include projections of future financial operations.

While the outlays of the Federal Reserve System are not explicitly shown in the federal budget, the net earnings of the System--total income less operating expenses--are reflected in the federal budget totals. This results from the System's weekly transfer of its net earnings to the U.S. Treasury, which are recorded as "miscellaneous receipts" in the revenue side of the budget. The net earnings of the Federal Reserve System have grown substantially in recent years as its portfolio of U.S. government securities has expanded and interest rates have risen. For fiscal year 1983, total transfers of earnings by the Federal Reserve amounted to $14.5 billion, about equal to the total amount of receipts from estate and gift taxes and customs duties.

Because Federal Reserve income from portfolio earnings greatly exceeds operating expenses, financing of these expenses from other revenue sources is unnecessary. Annual appropriations approval of Federal Reserve spending plans is not required, a result of a provision of the Federal Reserve Act which stipulates that the Board's assessment "shall not be construed to be Government funds or appropriated moneys."

The History of the Federal Reserve's Budgetary Independence

The Federal Reserve System has never been subjected to the appropriations process, and aside from the recording of transfers of Federal Reserve earnings as budget receipts, its financial operations have always been excluded from the federal budget. This insulated budgetary status has enabled the Federal Reserve to make decisions with relative independence from Congressional and Presidential influence. A review of the 70-year history of the Federal Reserve (see Chapter II) indicates that the relationships between the Federal Reserve's functions and its independence have varied over time.

When the Federal Reserve Act was being considered, it was generally agreed that establishing an institution with the power to provide liquidity to the banking system would make financial crises less likely. The structure of this proposed institution, however, was highly controversial. Although some favored a strong central bank located in Washington under the control of the President, others wanted the Federal Reserve to be independent of the executive branch and controlled by private bankers. Widespread concern about the influence of New York as a financial center favored a regional structure. The Federal Reserve System as it emerged was a complex mixture of these opposing elements, and its budgetary status was representative. The Banks, being privately capitalized, were thought to be out of the purview of the annual appropriations process (although the act did establish a franchise tax on the Banks' profits). The Board of Governors required no appropriations, having been given the right to assess the Federal Reserve Banks for coverage of expenses.

Two decades after the creation of the Federal Reserve System, the Federal Reserve Act was significantly modified in 1933 and 1935. These laws responded to the problems of monetary management in the Great Depression by formally establishing the Federal Open Market Committee. As power was centralized in the System, the Board of Governors was also given greater independence from the executive branch by elimination of the ex officio memberships of the Secretary of the Treasury and the Comptroller of the Currency. The franchise tax on Bank profits was repealed and the language which defined Board assessments as non-governmental funds was added. The fees received by the Comptroller of the Currency and the Federal Deposit Insurance Corporation were protected with similar language. The purpose was to partially insulate commercial bank regulation and monetary policy from the political process.

While no significant changes in the Federal Reserve's budgetary status were made legislatively from the mid-thirties until 1978, several important changes were made without legislation. In 1947, the Federal Reserve decided to transfer most of its profits to the Treasury after Members of Congress expressed interest in requiring the Federal Reserve to do so. At this time, the Federal Reserve was beginning to conduct monetary policy differently than it had in the past. Until the end of World War II, the main goal of monetary policy was to support Treasury financing by keeping interest rates low. As inflation threatened during the post-World War II and Korean War periods, the Federal Reserve made price stability an additional goal of monetary policy. The emphasis on price stability as a monetary policy goal strengthened the case for the budgetary independence of the Federal Reserve, since the interest-rate policies required to promote price stability could be unpopular with the President or the Congress.

This case for budgetary independence was accepted by the President's Commission on Budget Concepts, which recommended in 1967 that the Federal Reserve be excluded from the new "unified budget." This budget consolidated almost all government spending accounts into a single budget. The Commission gave three reasons for its exclusion of the System from the unified budget. It believed that inclusion would constitute an announcement of future monetary policy, thus jeopardizing the flexibility and independence of the monetary authorities. Second, projections of future System operations--which would be required if the Federal Reserve was included in the budget--did not appear feasible at that time. Third, the Commission believed that the nature and significance of Federal Reserve Bank receipts and expenditures were different from those of most other government programs and activities.

The case for the Federal Reserve's budgetary independence has not been universally accepted. Some believe that monetary policy goals should be determined by officials accountable to the public through elections, and therefore see no need for budgetary independence. Others maintain that the Federal Reserve has been allowed to make expenditures that would not be permitted for other agencies only because of its exemption from the annual appropriations process and its exclusion from the budget.

The Congress has responded to these accountability and spending control concerns recently, but only to a limited degree. Several laws of the mid-1970s required the Federal Reserve to report periodically on economic conditions and policy goals. The Congress also reviewed and directed Federal Reserve spending through authorizing legislation and oversight. In 1978, it gave the General Accounting Office the right to audit all Federal Reserve System activities except monetary policy and foreign account activities. In 1980, full recovery of the costs of certain payments services was required by the Monetary Control Act. The Senate Banking Committee held annual oversight hearings on the budgets of the Federal Reserve from 1977 to 1980.

BUDGETARY ACCOUNTABILITY AND INDEPENDENCE

From time to time, proposals are made to increase the budgetary accountability of the Federal Reserve. These proposals would have varying effects on the Federal Reserve's independence. This report does not attempt to determine the correct balance between the Federal Reserve's independence and its budgetary accountability. It simply presents information relevant to choices that would affect the balance.

The proposal that would reduce Federal Reserve independence the least would be complete presentation of the finances of the System in the Budget of the U.S. Government. This proposal is discussed in detail in Chapter IV. The proposal that would reduce independence the most would be a requirement that Federal Reserve expenditures be approved in advance through the Congressional appropriations process. Another budgetary accountability proposal would be the conduct of annual oversight of the Federal Reserve's budget and the stipulation of budget savings in authorizing legislation. Appropriations, authorizing legislation, and oversight are discussed in detail in Chapter V.

Complete Budget Presentation

One method of increasing budgetary accountability would be to include the complete finances of the Federal Reserve System in the Budget of the U.S. Government. The Federal Reserve would provide data on actual and projected income and expenses by program and type. This approach would make its budgetary transactions visible to the public and readily comparable to the transactions of other government agencies. It would also make the U.S. government's "unified budget" more comprehensive.

A not uncommon belief is that complete budget presentation of the Federal Reserve System finances is precluded by the private characteristics of the Federal Reserve Banks. These characteristics are member bank ownership of capital subscriptions to the Federal Reserve Banks and participation in selection of bank directors. The Board of Governors exercises significant control over the Banks' policies, budget, and personnel, however. Moreover, the Federal Reserve Banks' activities--especially in the monetary and regulatory policy areas--are governmental in character. After a review of these public characteristics, the President's Commission on Budget Concepts wrote, "The System is clearly a Federal Government Operation."

Of the three methods of increasing budgetary accountability, budget presentation of the Federal Reserve's administrative expenses would have the least effect on the Federal Reserve's independence. The Federal Reserve would remain free to determine its own administrative expenses. If the Federal Reserve's expenses were visible, however, proponents of less government spending might consider more readily the possibility of reductions in Federal Reserve spending. Almost all other independent agencies are included in the budget documents despite a similar threat to their spending flexibility. The Federal Reserve would need to expand its accounting and budgeting systems to conform with the federal system.

Budget presentation of Federal Reserve finances could be confined to its administrative expenses, or could include its future monetary policy finances as well. The potential impact on the Federal Reserve's independence would be greater if the Federal Reserve was required to provide specific projections of its earnings. Projections of Federal Reserve earnings are made from point estimates of interest rates and of the size and maturity distribution of the Federal Reserve's portfolio. Revelation of the Federal Reserve's estimates of these factors would convey significantly more information about its policy intentions than is currently contained in the Federal Reserve's wide range estimates of money growth and interest rates. If it was required to publish a specific projection of its portfolio size, this could serve as a benchmark for evaluation of its monetary policy goals and performance.

Appropriations

A second method of increasing budgetary accountability for the Federal Reserve would be to subject the administrative expenses of the Board and the Reserve Banks to annual appropriation review. The operating budgets of most federal agencies are reviewed in the same manner, including those of the judiciary and most regulatory agencies. This approach would provide closer scrutiny of the System's operations--preparation of economic studies and statistics, provision of financial services, and supervision and regulation of banks. Many of these activities are similar to those performed by other federal agencies, and it is possible that some savings might be achieved through appropriations review.

The magnitude of potential budgetary savings from this approach is uncertain. Congressional review and approval of agency spending is thought to restrain agencies from spending funds wastefully. A limited review of the Federal Reserve's recent spending record (see Chapter V) suggests, however, that its spending does not appear to be significantly greater than those of other agencies with comparable functions. In other words, the Federal Reserve may already be following a relatively self-restrained spending policy, and review for management efficiencies might not produce significant budgetary savings.

On the other hand, should the Congress wish to ensure that the Federal Reserve's spending remain within the normal range for federal agencies, the appropriations process could be used for this purpose. The Congress could even reduce the Federal Reserve's spending below current levels by limiting the funds available to it, although significant budgetary savings would mean reductions in the level of services provided.

The principal issue raised by the application of the appropriations process to the Federal Reserve is whether the Congress should be involved in the determination and conduct of monetary policy. Carrying the appropriations process to its fullest would entail establishing appropriations ceilings on open-market, foreign currency, and discount loan transactions. Such ceilings could greatly reduce the Federal Reserve's operating flexibility, which is needed in the conduct of monetary policy in order to respond to unexpected economic or financial market conditions. Operating flexibility could be preserved by limiting such ceilings to the Federal Reserve's administrative expenses.

Even if appropriations were required only for administrative expenses, the process could be used to influence monetary policy through legislative riders or reduction of funding levels. The degree to which the Congress would use this power, and the effects on policy, are very uncertain. To determine monetary policy successfully, the Congress would need to set clear monetary policy goals that were achievable and consistent with other economic goals. The traditional focus of the appropriations process, however, is the control of agency expenditures, not economic goal-setting. Should the Congress decide to set monetary goals instead of delegating this responsibility to the Federal Reserve, it could do so more effectively through the use of authorizing legislation and an expanded budget and economic planning process.

Oversight and Authorizing Legislation

A third method of increasing budgetary accountability would be to conduct annual oversight of the Federal Reserve's budget and set mandatory budget savings in authorizing legislation. Annual oversight of System spending could be performed by the Banking Committees of the House and Senate, in a manner similar to that of hearings conducted by the Senate Banking Committee in the late 1970s. The GAO's audit role could be expanded by having it perform complete audits of the System's books, as it does now for other independent agencies. The GAO could also be asked to review System spending and judge its efficiency.

Authorizing legislation could be used to order savings in the Federal Reserve's budget, savings that would result from significant changes in the System's structure or programs. Recovery of the costs of supervision and regulation through the imposition of fees on banks--the general practice of the other depository institution regulatory agencies--is probably the greatest opportunity for savings in the Federal Reserve's budget. Savings could also be realized by extending the market test constraint of the Monetary Control Act to certain public and service programs that are now financed from current income. Consolidating certain activities of the three agencies that regulate commercial banks and bank holding companies--the Federal Reserve, the Comptroller of the Currency, and the Federal Deposit Insurance Corporation--could result in long-term savings, although significant transition costs would be incurred.

Use of authorizing legislation and oversight would be generally less of a threat to the Federal Reserve's independence than use of the appropriations process, although it could significantly affect Federal Reserve policies and finances. In the oversight process, committees are limited to review of expenditures after the fact or to suggestions for future spending, whereas the Congress may order specific spending levels for particular purposes in the appropriations process. Most authorizations are for a multiyear or unlimited time period, whereas appropriations are considered annually. These considerations, and a concern for the independence of regulatory policy, have led the Congress to use oversight and authorizing legislation in place of appropriations for three depository institution regulatory agencies--the Comptroller of the Currency, the Federal Deposit Insurance Corporation, and the National Credit Union Administration. Other financial regulatory agencies--the Federal Home Loan Bank Board, the Federal Savings and Loan Insurance Corporation, the Farm Credit Administration and the Securities and Exchange Commission--are subject to the appropriations process. None of these agencies have charges similar to the monetary policy responsibilities of the Federal Reserve. On the other hand, agencies with policy responsibilities comparable in importance to monetary policy, such as the Department of Defense, are subject to the appropriations process.

CHAPTER I. INTRODUCTION

Central banks are unusual instititutions. They make very important economic policy decisions, yet they are often formally independent from the elected officials of their governments. The central bank of the United States, the Federal Reserve System, is no exception. Its Governors are appointed by the President and confirmed by the Senate for 14-year terms, but are secure from removal except for cause. In general, its expenditures are not reported in the *Budget of the U.S. Government*, and no advance approval from the President and the Congress to expend funds is required. In its most important area of responsibility--the determination and conduct of monetary policy--the President and the Congress have traditionally declined to curb it formally with executive orders or legislation.

The Federal Reserve and other central banks are not wholly independent from government influence, however. 1/ Governments usually appoint central bank directors and often own 100 percent of central bank stock. The economic policies of governments and central banks are usually more closely aligned than might be expected given the central banks' formal independence, reflecting the frequent consultations that are common practice. Central banks often turn over their profits to the government treasury. Some central banks must submit their budgets to the government executive for review (in Japan the Ministry of Finance must approve the Bank of Japan's budget). No banks, however, are required to forward their budgets to parliaments for approval.

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1. Sources addressing the varying independence of central banks include: Don Fair, "The Independence of Central Banks," *The Banker*, vol. 129 (October 1979), pp. 33-41; Patricia Wertman, "The Bank of England and the Federal Reserve System: A Brief Comparison," *Congressional Research Service* (September 18, 1981). "Central Banking Arrangements in Selected European Countries," *International Currency Review*, vol. 12 (1980), pp. 19-23; Commission of the European Communities, Monetary Committee, *Monetary Policy in the Countries of the European Economic Community* (1972); Bank for International Settlements, *Eight European Central Banks* (Praeger, 1963); David L. Grove, "Central Bank Independence and the Government—Central Bank Relationship," International Monetary Fund (April 2, 1952).

There are, of course, important differences between the U.S. system of government and the parliamentary systems of other countries. The Congress is the most active and powerful of the legislatures in developed countries, and its power of the purse is especially notable. 2/ One of the major activities of the Congress is the annual review of spending by government agencies and authorization of their plans for future spending. These plans are submitted to the Congress at the beginning of each calendar year in a comprehensive budget document prepared by the President. The Federal Reserve is one of the few agencies that are exempt from Congressional review.

The apparent anomaly created by these two traditions--the formal independence of central banks and the comprehensive review of agency spending by the Congress--is the subject of this report. Chapter II provides a history of the independent budgetary status of the Federal Reserve. Chapter III is an overview of the Federal Reserve's current structure, activities, and financing. Chapters IV and V consider in detail two possible changes in the budgetary status of the Federal Reserve: complete presentation of its finances in the Budget of the U.S. Government, and a requirement of prior appropriations for the Federal Reserve's administrative expenditures. Appendix A compares the budget presentation of the Federal Reserve to that of other agencies, and Appendix B describes the Federal Reserve's budgeting system. The report does not consider the advantages and disadvantages of the Federal Reserve's monetary policy independence in itself.

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2. Michael L. Mezey, Comparative Legislatures (Duke University Press, 1979); Gerhard Loewenberg and Samuel C. Patterson, Comparative Legislatures (Little, Brown, 1979); David Coombes, ed., The Power of the Purse: The Role of European Parliaments in Budgetary Decisions (George Allen and Unwin, 1976).

CHAPTER II. A HISTORY OF THE BUDGETARY INDEPENDENCE OF THE FEDERAL RESERVE SYSTEM

In its early history, the United States created and subsequently abolished two central banks. Its third central bank, established in 1913, was given extensive powers. The Federal Reserve System controls the money supply, regulates and supervises certain banks and bank holding companies, serves as a source of liquidity to depository institutions, operates check clearing, payments mechanism, and currency facilities, and acts as fiscal agent for the U.S. government.

These activities are based upon broad delegations of authority from the Congress to the Federal Reserve System. Article 1, Section 8, Clause 5 of the Constitution grants to the Congress the power "to coin money, regulate the value thereof, and of foreign coin. . . ." The Congress, however, has delegated this power in the main to the Federal Reserve and in a limited way to the Treasury Department. The Congress has been more active in other areas of the Federal Reserve System's responsibilities, such as the regulation of depository institutions through regular amendments to the banking laws. 1/ Nevertheless, the Federal Reserve System's independence within the government is well-established, including its ability to finance its expenditures from its earnings. Because the Federal Reserve System does not depend on annual appropriations, it is not subject to a process by which the Congress could annually limit and direct its activities. Its off-budget status has reduced the visibility of its expenditures, thus decreasing interest in control of these expenditures. This chapter recounts the complex historical record of the Federal Reserve's budgetary independence.

THE FEDERAL RESERVE ACT

The Federal Reserve System was established by the Federal Reserve Act of 1913 (P.L. 63-43). Central to its creation was the desire for an efficient payments system—a system for the reliable transfer of funds, payments, and money among financial institutions across the country. Until then, holders of checks written on banks in far-off cities had to rely on

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1. Congressional Research Service, A Reference Guide to Banking and Finance (March 1983); Formation and Powers of National Banking Associations (May 1983).

clearing services provided by correspondent banks. Because these services were time-consuming and costly, checks presented on out-of-town banks were often discounted from their full value. During financial panics, commercial transfers of funds were extremely difficult to carry out.

A related purpose of the Federal Reserve System was the provision of an elastic money supply—one that would be responsive to the seasonal needs of trade. At the time, for example, the assets and liabilities of the rural banks varied considerably from one time to another depending on the credit needs of the agricultural sector. When rural banks needed cash, they often drew down their sizable deposits with city banks. The resultant illiquid conditions of city banks often precipitated reductions in the money supply and financial panics. Other variable demands for currency and credit, particularly from the financial activities of the Treasury, had similar results.

The Federal Reserve Act granted major powers to the System, including the powers to:

- Receive and transfer gold;
- Distribute currency ("Federal Reserve Notes");
- Settle and pay the obligations of member banks to each other;
- Advance funds to member banks;
- Establish reserve requirements for member banks;
- Examine and supervise member banks;
- Serve as the fiscal agent for the Treasury; and
- Purchase and sell government securities and other eligible paper on the open market.

To carry out these activities, the Federal Reserve Act created the Federal Reserve Banks and the Federal Reserve Board, collectively known as the Federal Reserve System. Federal Reserve Banks were established in 12 Federal Reserve districts across the country. The Banks, chartered as federal corporations, were capitalized with subscriptions from private banks, which in return became members of their Banks and eligible for Federal Reserve System services. A Federal Reserve Board of seven Presidentially appointed members, including the Secretary of the Treasury (as *ex officio* Chairman) and the Comptroller of the Currency, was established to oversee the activities of the Banks. Directors of the Banks were selected by both the Board and members. Most of the Federal Reserve System's activities were carried out by the Banks, but the Board had supervisory control of the Banks. The mixed private-public ownership and regional structure of the System reflected the traditional hostility in the United States toward the concentration of banking powers in a "central bank." 2/ Similarly, the Secretary of the Treasury and Comptroller of the Currency served on the Board to prevent the private "Money Trust" from controlling the System, but in an ex officio capacity in order to limit executive branch influence on a constitutionally prescribed legislative function. 3/

The expenses of the Banks were to be financed from earnings, and the Board was given the power to assess the Banks for coverage of its expenses. The Congress retained the power to set ceilings on the level of Governors' salaries. The Federal Reserve Act also established a "franchise tax," which mandated the transfer of one-half of the Banks' net income to the Treasury. The other half could be added to the surplus of the Banks, subject to a ceiling of 40 percent of the paid-in capital of member banks. Ninety percent of net income was to be due the Treasury following the attainment of the targeted surplus.

The legislative history of the Federal Reserve Act's grant of financial independence to the System is unclear. The Secretary of the Board in its early years, H. Parker Willis (who also helped write the Federal Reserve Act as a Congressional staff member), wrote in 1923:

> Even within the very first few weeks after the organization of the Board had been set up, there came to it memoranda and letters from politicians hinting at the desirability of concessions when the Board's annual appropriations came before Congress for adoption. Those who wrote in this manner had overlooked the fact that the Federal Reserve Act had carried an inconspicuous provision authorizing the Federal Reserve Board to obtain the necessary money for its expenses by assessing the federal reserve banks.... It may be doubted whether Congress or the Administration had recognized the importance of this provision and the significance of the independence that it might bestow

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2. See the July 10, 1832, veto message of President Jackson on the bill for recharter of the Second Bank of the United States.

3. The Federal Reserve Banks were also given the responsibility of holding Treasury accounts, a reaction to previous instances of manipulation of these accounts for political purposes.

> upon the Board, but it served an excellent purpose in the early years of the system by enabling the Board to withstand much of the pressure both from Congress and the executive branch of the Government. 4/

The Congress did realize, however, that the Federal Reserve Banks were likely to be profitable. The House report on the Federal Reserve Act contained the following justification of the franchise tax:

> . . . It has frequently been asked why the Government should be allowed to share in the earnings of Federal reserve banks at all. There are two reasons of conspicuous and obvious character why it should do so: (1) It vests the Federal reserve banks with the sole and exclusive function of note lending, from which all other banks are debarred; (2) it places the public funds with the Federal reserve banks to an amount certainly vastly larger than that of any other depositor and equal to the combined deposits of large groups of banks. The distribution of earnings upon the basis of deposit balances would give to the Government a large share of the profits in any case and when the present national-bank notes shall have been replaced by Federal reserve notes it is obvious that the function of note issue will result in a large volume of earnings which the Federal reserve banks could not enjoy were they to share this power with other banking institutions. To a substantial share in this earning, leaving for the reserve banks only a fair compensation for their services in taking out the notes, the public is evidently entitled. 5/

Given that the Banks were projected to earn income, appropriations for the Federal Reserve Board were not necessary as a source of financing. 6/

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4. H. Parker Willis, The Federal Reserve System: Legislation, Organization, and Operation, quoted in A. Jerome Clifford, The Independence of the Federal Reserve System (Oxford University Press, 1965) pp. 83-84.

5. House Banking and Currency Committee, House Report 69, 63rd Congress, pp. 38-39.

6. See also Richard H. Timberlake, The Origins of Central Banking in the United States (Harvard University Press, 1978).

THE BANKING ACTS OF THE 1930s

Contraction of the financial system in the Great Depression stimulated the passage of two landmark banking laws, the Banking Act of 1933 (P.L. 73-66) and the Banking Act of 1935 (P.L. 74-305). These acts established the Federal Deposit Insurance Corporation (FDIC) and prohibited the participation of banks in the securities, real estate, and insurance industries.

The Banking Acts also increased the power and autonomy of the Federal Reserve Board (renamed the Board of Governors of the Federal Reserve System in 1935) relative to the Federal Reserve Banks and the Treasury. The acts removed the Secretary of the Treasury and the Comptroller of the Currency from the Board, increased the size of the Board to seven voting members, and lengthened terms of office from 10 to 14 years. The Board was also given the authority to approve the chief operating officers (President and First Vice President) of each Bank.

Crucial to the restructuring of the system was the gradual discovery of the earnings and money creation powers of open-market operations. In 1913, the Congress considered the discount window to be the Federal Reserve System's most powerful tool, but the purchase of securities by Federal Reserve Banks in the 1920s proved otherwise. The purchases were primarily intended to increase Bank earnings (earnings from other sources were low), yet they also increased the supply of money and lowered interest rates. Treasury borrowing costs were thereby reduced, as were returns on the investments of Treasury trust accounts and member banks. Because purchases by individual Federal Reserve Banks were uncoordinated, the market for Treasury securities was often disorderly. Criticisms from the Treasury and member banks led to creation in 1922 of an advisory Open Market Investment Committee of the five largest Banks. Purchases and sales of securities in the mid-1920s by the Federal Reserve Bank of New York for the Committee, under the influence of the Treasury Department and other Reserve Banks, showed how money creation through open-market activities could affect the business cycle. The Committee was replaced by the Open Market Policy Conference in 1930, with an expanded membership of all twelve Federal Reserve Banks and the Chairman of the Federal Reserve Board as convenor. The 1933 Banking Act formally recognized the Conference as the Federal Open Market Committee, but in 1935 the Federal Reserve Banks were stripped of complete control of open-market operations. Seven of the Federal Reserve Bank members were replaced by the Board of Governors (who thus formed a bare majority of the 12-member Federal Open Market Committee).

Increased budgetary independence for the Federal Reserve System was another result of the Banking Acts. The franchise tax was repealed and the

General Accounting Office lost the power to audit the Board. Federal Reserve Board assessments on Federal Reserve Banks were insulated from direct control by elected officials by language that required that "funds derived from such assessments shall not be construed to be Government funds or appropriated moneys." This provision overturned a 1914 Ruling of the Attorney General which construed the assessments as "Public Moneys" subject to regular audits. In return for this freedom, the Federal Reserve System transferred half of its surplus ($139 million) to partially capitalize the FDIC. 7/

These changes in the Federal Reserve System's powers were the result of numerous and somewhat contradictory opinions of the previous performance and proper functions of the system. The "central" bank status of the System was weak because of the influence of the Federal Reserve Banks on System policy. Open-market activities of the System had been counterproductive during the early 1930s when the Reserve Bank-dominated Open Market Policy Conference pursued an insufficiently expansive monetary policy. On the other hand, the influence of the Treasury on Federal Reserve System purchases of securities was believed to foster inflation; a similar threat was posed by populist support in the Congress for easy money. 8/ The solution chosen for these problems was a government-controlled central bank "independent" of political influence. A contributing factor was the enhanced responsibility of the Federal Reserve System to ensure the safety and soundness of member banks.

THE "ACCORD"

The "independence" of the new Federal Reserve System, however, was only relative to its past, for the Treasury retained substantial influence over the System's activities. During the Depression, the Federal Reserve System regularly supported Treasury offerings. During World War II, it "pegged" interest rates at a range from three-eighths of 1 percent on Treasury bills to 2.5 percent on long-term bonds. As described by Herbert Stein,

> That meant that the Federal Reserve would buy those securities whenever necessary to keep their prices from falling

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7. Clifford, The Independence of the Federal Reserve System, p. 355n.

8. Milton Friedman and Anna Jacobson Schwartz, A Monetary History of the United States, 1867-1960 (Princeton University Press, 1963), p. 445.

> and their yields from rising. But when the Federal Reserve bought securities it increased reserves of the banking system and so permitted an expansion of the money supply. As long as it remained committed to supporting the prices of government securities the Federal Reserve could not control the money supply in the interest of any other objective—such as to stabilize the price level. 9/

By 1943, one-half of the Federal Reserve System's employees were engaged in fiscal agency activities (war bonds and Treasury securities). 10/

Earnings from open-market operations relative to expenses grew rapidly during the war. By 1946, the Federal Reserve System earned $150.4 million, but paid only $67,054 to the Treasury. After this transfer, making accounting adjustments, covering expenses of the Board and the Banks, and paying dividends to member banks, the System added $81.5 million of remaining income to its surplus. As the Congress and the Treasury considered amending the Federal Reserve Act to require the System to turn over some of its earnings to the Treasury, the Federal Reserve System preempted any order by "voluntarily" deciding to pay "interest on Federal Reserve notes" in the amount of approximately 90 percent of its earnings, citing Section 16 of the Federal Reserve Act as authority. 11/ As a result, in 1947 only $8.4 million was transferred to surplus, and $75.2 million was paid to the Treasury as income on Federal Reserve notes. 12/ Shortly thereafter, the Federal Reserve ended support of the 3/8 percent rate on Treasury bills. 13/

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9. Herbert Stein, Presidential Economics (Simon and Schuster, 1984), p. 82.

10. Clifford, p. 188.

11. This percentage was similar to the amount required under the repealed franchise tax.

12. Additions to surplus are now made to bring the surplus equal to the level of paid-in capital from member banks. Payments of interest on Federal Reserve notes have accelerated rapidly with rises in nominal interest rates, amounting to $14.2 billion in 1983.

13. Friedman and Schwartz, pp. 578-79n. See also Walter E. Spahr, "Federal Reserve Out of Bounds Again," Commercial and Financial Chronicle (June 19, 1947), pp. 2, 31, and Spahr, "More on Reserve Board's Illegal Distribution of Federal Reserve Banks' Earnings," Commercial and Financial Chronicle (September 18, 1947), pp. 1, 22-24.

With an increase in the rate of inflation during the Korean War, the Federal Reserve System formally ended its support of Treasury financing in 1951, having gradually reduced its support since 1947. The Federal Reserve Act's relatively unspecific delegation of authority to the Federal Reserve System did not require it to support Treasury financing, but President Truman, among others, expected it to do so. Following the example of President Franklin D. Roosevelt in 1937 (when he successfully "hoped" that the Federal Reserve System would cooperate with the Treasury Department's gold sterilization program), Truman called the Board of Governors to the White House to request support of long-term Treasury bonds at low rates. The Federal Reserve System was largely successful in resisting his request, for support in Congress for ending the pegging policy was strong. The result of the conflict became known as the "Accord," which simply stated the principle that:

> The Treasury and the Federal Reserve System have reached full accord with respect to debt-management and monetary policies to be pursued in furthering their common purpose to assure the successful financing of the Government's requirements and, at the same time, to minimize monetization of the public debt.

The Federal Reserve System gradually exercised its new flexibility to limit inflationary pressures over the succeeding years, with the assent of the Eisenhower Administration. 14/

THE MARTIN-PATMAN YEARS

For two decades after the Accord, the issue of the Federal Reserve System's independence was dominated by two individuals: William McChesney Martin, the Chairman of the Board of Governors from 1951 to 1970, and Representative Wright Patman (D-TX), chairman of a Joint Committee on the Economic Report subcommittee in the 1950s and Chairman of the House Banking Committee from 1963 to 1974. Martin was a strong advocate for the System's independent exercise of monetary and credit powers. Patman was the System's foremost critic and a tireless proponent of bringing the System under direct Congressional control. During landmark hearings on the Federal Reserve System in 1964, 15/ Patman pro-

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14. Friedman and Schwartz, p. 625.

15. Subcommittee on Domestic Finance, House Committee on Banking and Currency, The Federal Reserve System After Fifty Years (1964).

posed legislation that would retire the stock of Federal Reserve Banks, make the Secretary of the Treasury the chairman of the Board of Governors, mandate the deposit of all System earnings in the Treasury, require prior appropriations for System expenditures, and make Federal Reserve support of Treasury securities mandatory with a ceiling for short-term securities of 4.25 percent.

None of these proposals was adopted, despite the expanded role played by the Federal Reserve System in economic policy. In the Employment Act of 1946, the government had declared its willingness "to promote maximum employment, production, and purchasing power." The Eisenhower Administration believed that purchasing power could be protected only if money creation (Federal Reserve System) and debt management (Treasury) were carried out by separate institutions. In the words of Chairman Martin, the Federal Reserve was supposed to be "taking the punch bowl away just when the party is getting merry . . .," and could do so only if its day-to-day operations were free from direction by the Congress and the Treasury.

In actuality, the System paid great attention to elected officials during the 1950s and 1960s. Consultation with the Executive Branch was extensive, and Congress often held oversight hearings. 16/ Those who preferred to see the Federal Reserve System conduct policy with the single goal of preventing inflation were disappointed, for it often allowed the money supply to grow rapidly during this period. It participated heavily in Treasury financings, such as the 1952 Treasury refunding. Public statements of independence notwithstanding, many thought that by taking these actions the Federal Reserve System was responding to the desires of elected officials. 17/

The budgetary independence of the Federal Reserve System was bolstered by the recommendation of the 1967 President's Commission on Budget Concepts, which was that only the profits of the Federal Reserve Banks that were transferred to the Treasury be included in the new "unified budget." The Commission stated its belief that:

> Inclusion of the Federal Reserve Banks in the federal budget might jeopardize the vital flexibility and independence of the monetary authorities. Moreover, projections of System opera-

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16. Major inquiries were made in 1950, 1951, 1952, 1954, 1957, 1959, 1960, 1964, and 1968.

17. G.L. Bach, Making Monetary and Fiscal Policy (Brookings, 1971), pp. 158-68.

> tions for a forward period—as would be required if included in the budget—do not appear feasible at the present time. The nature and economic significance of Federal Reserve Bank "receipts" and "expenditures" are different from those of most other government programs and activities. 18/

(See Chapter IV for an analysis of the Budget Concept Commission's arguments.)

THE RECENT DECADE

For the most part, the Federal Reserve System retained its budgetary and policymaking independence during the 1970s. Several laws were adopted that affected its monetary policy responsibilities, audits of its expenditures, and the provision of services to the banking industry.

Legislation increased the monetary-policy reporting duties of the Federal Reserve System to the Congress. H. Con. Res. 133 of the 94th Congress, passed in 1975, required the Federal Open Market Committee (FOMC) to make public annual targets for growth in the money supply and also required periodic testimony by the Chairman of the Board of Governors before the Banking Committees. Subsequently, these provisions were made a statutory requirement in P.L. 95-188, the Federal Reserve Reform Act of 1977. The Full Employment and Balanced Growth Act of 1978 (P.L. 95-523, also known as the Humphrey-Hawkins Act) ordered the FOMC to determine whether its monetary targets were consistent with the economic objectives (for output, employment, and prices) of the President. Another law protected the System from similar "oversight" by the executive branch. P.L. 93-495 enjoined the Office of Management and Budget or any other agency from requiring advance approval of Federal Reserve System testimony or legislative recommendations.

Two laws affecting Federal Reserve System expenditures and revenues were enacted during this period: the Federal Banking Agency Audit Act of 1978 (P.L. 95-326) and the Monetary Control Act of 1980 (P.L. 96-221). The Audit Act gave the General Accounting Office the authority to audit the Federal Reserve System, the Federal Deposit Insurance Corporation, the Comptroller of the Currency, and the Financial Institutions Examination Council. Federal Reserve System activities excluded from audits were:

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18. Report of the President's Commission on Budget Concepts (1967), p. 28.

1. Transactions for or with a foreign central bank, government of a foreign country, or nonprivate international financing organization.
2. Deliberations, decisions, or actions on monetary policy matters, including discount window operations, reserves of member banks, securities credit, interest on deposits, and open-market operations.
3. Transactions made under the direction of the Federal Open Market Committee; or
4. A part of a discussion or communication among or between members of the Board of Governors and officers and employees of the Federal Reserve System related to clauses (1)-(3) of this subsection.

The Monetary Control Act required the Federal Reserve System to charge depository institutions for certain of its financial services. This provision was part of a complex banking law, the Depository Institutions Deregulation and Monetary Control Act of 1980. In the past, these services were provided "free of charge," but only to members of the Federal Reserve System. As a condition of membership, banks had to reserve a portion of their assets as non-interest-earning reserves—an implicit charge for services. Non-member institutions could use Federal Reserve System services, but only through "correspondent banks" that demanded similar non-earning deposits in return.

With the rise of nominal interest rates in the 1970s, however, the cost to members of non-interest-bearing reserves grew. In the "dual banking system" of the United States, national banks can withdraw from the Federal Reserve System by converting to state charters. State members can withdraw by giving notice. A decline in the percentage of bank assets held as reserves in the Federal Reserve System that resulted from withdrawals from membership was thought to threaten monetary management. The Monetary Control Act solution to the "membership problem" was to lower levels of required reserves and to extend reserve requirements to all types of depository institutions. In return, Federal Reserve System services were made available to non-member depository institutions.

The costs of providing services were to be recovered through fees for the following services:

- Currency and coin;
- Check clearing and collection;
- Wire transfer;
- Automated clearinghouses;
- Settlement;
- Securities safekeeping;
- Float; and
- Any new services, including but not limited to electronic funds transfer.

Fees were to be phased in, and established on the basis of direct and indirect costs, including an imputation of the amount of taxes paid by and a return to capital earned by private business firms. Float prices were to be priced at the federal funds rate, The System was granted the latitude to price so as to provide an adequate level of services nationwide.

Finally, several committees reviewed the expenses of the Federal Reserve System. Most prominent was a series of Senate Banking Committee hearings from 1977 to 1980. These hearings were in the format of an appropriations hearing (although Federal Reserve System expenditures did not need to be approved by the Banking Committee in advance). Federal Reserve System justifications were less detailed than regular appropriations justifications, but Chairman Proxmire was able to question Governor Philip Coldwell, Chairman of the Board's Committee on Federal Reserve Bank Activities (which oversees Federal Reserve Bank budgets), on the purposes of particular items and on the Federal Reserve System's plans for future spending. Hearings on the Federal Reserve System were also held by the Senate Banking Committee in 1981. These hearings considered among other bills S. 1691, which would have required prior appropriations for System expenditures and the deposit of its gross income in the Treasury.

SUMMARY

The independence of the Federal Reserve System is not constitutionally based, as is that of the judiciary. Rather, it has been granted to the System by the Congress. The history of this independence is not a simple one, in part because the concept of "independence" is itself complicated. A distinction between "formal" and "behavioral" independence should be made. 19/ The Federal Reserve has a great deal of formal independence, given the set tenure of its executives, its broad authorizing legislation, its limited presentation in the budget, and its statutory exemption from the appropriations process. Its behavioral independence--its freedom to follow policies counter to the preferred policies of the President and the Congress--may be more limited. The reason for this is simple--the Federal Reserve operates in a democracy where great value is placed on the accountability of government agencies to elected officials and the public. A 1965 study of the independence of the Federal Reserve provided the following description of this limitation:

> . . . the Federal Reserve System was constructed on the general principle that the government could not be trusted to exercise directly, through ordinary executive or legislative channels, the monetary power which was part of its sovereignty. Three reasons might explain the adoption of this principle. First, the government was not to be expected to pursue a monetary policy in vigorous fashion, especially when a restrictive policy was demanded. Hence, it would not oppose sufficiently a strong upsurge of inflationary forces. Second, wisdom and prudence seemed to demand that the borrowing and lending functions involved in the financing of the government should not be combined in a government organization directly responsible to the electorate. Such an arrangement would make it very difficult for the government to carry out actions which in their immediate effects would be unpopular with the electorate. The government was not likely to pay a relatively high current market rate of interest when it had authority as lender to bring the rate down to a more popular acceptable level. Accordingly, a buffer organization was needed. Third, the area of money and banking required a specialized and erudite knowledge traditionally not expected of the government.
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> As the Federal Reserve System grew in experience and stature, it did not reject this principle of no-trust in the government. In fact, the Federal Reserve frequently was somewhat doctrinaire in upholding the principle. At the same time the System became more aware that it was not self-sufficient. It could not properly coordinate its actions with those of the government unless it recognized and accepted the power, the

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19. John T. Woolley, Monetary Politics: The Federal Reserve and the Politics of Monetary Policy (Cambridge University Press, 1984), pp. 10-15.

> interest, and the honorableness of the Treasury and the Administration in monetary affairs. Only by so doing would its independence be recognized and accepted. In addition, Congress was ever fearful lest the Federal Reserve would try to go its own way, promote the interests of special groups, and neglect the welfare of all other groups and sections of the nation. The dangers of government abuse were no greater than those of neglect of the wishes of government. Hence questions were raised whether the Federal Reserve provided an institutional arrangement which was a happy medium between the conflicting dangers. 20/

As questions were raised about the Federal Reserve's independence, legislative proposals to restrict its formal independence were introduced. By and large, these proposals failed. It seems unlikely, for example, that Representative Patman would be satisfied with the legislation of the 1970s compared to his bills of 1964. Proposals to make the System subject to Presidential direction—from the 1949 Hoover Commission, the 1961 Commission on Money and Credit, and others—were also rebuffed. One explanation of the failure of Congress to adopt these proposals is simply that the Congress accepted the case for insulation of the Federal Reserve as described above by Clifford. According to this view, the Humphrey-Hawkins reporting process is seen as an appropriate method of Congressional involvement in monetary policy--appropriate in part because the Congress's role is limited. 21/

Another possible explanation is that the Federal Reserve has forestalled reduction of its formal independence by limiting its behavioral assertion of this independence—that is, it has allowed the money supply to grow or contract more rapidly than it would prefer, consistent with the wishes of the President or the Congress. Several empirical studies have concluded that the Federal Reserve has been generally responsive to the President's

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20. Clifford, pp. 33-35. See also Ralph C. Bryant, Money and Monetary Policy in Interdependent Nations (Brookings, 1980), pp. 318-33.

21. Steven M. Roberts, "Economic Policymaking in the United States: New Procedures Under Humphrey-Hawkins," Journal of Economic Dynamics and Control, vol. 1 (1979), pp. 271-82.

economic program in the post-World War II period. 22/ These studies are limited, however, by the great difficulty of accurately determining the preferred monetary goals of the President, the Congress, and the Federal Reserve. Others have suggested a "scapegoat theory." Its central assumption is that elected officials find it useful to retain the formal independence of the Federal Reserve so that they are shielded to some degree from blame for some of the costs of anti-inflation policies, while knowing that certain legal and practical restraints make the Federal Reserve responsive in a general way to the economic goals of the President and the Congress. 23/

Other studies suggest that the Federal Reserve has been able to determine and conduct monetary policy with relative freedom. These studies emphasize the highly technical nature of monetary policy and the sporadic interest of the Congress in monetary policy. 24/ They also note that the belief that the Federal Reserve Banks are wholly private entities, widely held in the early years of the System, has protected it from threats to its formal independence. 25/

The budgetary independence of the Federal Reserve has not been emphasized in analyses of its behavioral independence. Formal budgetary independence is often justified as a means of protecting the independence of the Federal Reserve in its monetary policy activities. The connection between budgetary independence and monetary policy flexibility was weaker at the Federal Reserve's creation than it is at present, however. In the early history of the System, changes in the amount of money in the economy

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22. Robert W. Weintraub, "Congressional Supervision of Monetary Policy," Journal of Monetary Economics, vol. 4 (April 1978), pp.341-62; Nathaniel Beck, "Presidential Influence on the Federal Reserve in the 1970s," American Journal of Political Science, vol. 26 (August 1982), pp.415-45.

23. Edward J. Kane, "Politics and Fed Policymaking," Journal of Monetary Economics, vol. 6 (1980), pp. 199-211.

24. Woolley, Monetary Politics; John F. Chant and Keith Acheson, "Mythology and Central Banking," Kyklos, vol. 26 (1973), pp.362-79; James L. Pierce, "The Myth of Congressional Supervision of Monetary Policy," Journal of Monetary Economics, vol. 4 (1978), pp. 363-70.

25. Michael D. Reagan, "The Political Structure of the Federal Reserve System," American Political Science Review, vol. 55 (March 1961), pp. 64-76.

were not used as a macroeconomic policy instrument. Maintaining price stability through control of the money supply did not become a generally accepted policy goal until after World War II; by that time the Federal Reserve System's budgetary independence was established.

Other factors have contributed to the formal budgetary independence of the Federal Reserve. The Federal Reserve System has often accommodated the express desires of the Congress in regard to its programs and spending—a notable example being the 1947 deposit of earnings. Misgivings about the possibility of political interference in the regulation and supervision of banks favored a grant of budgetary independence in 1933. Similar misgivings insulated the FDIC and Comptroller of the Currency from the appropriations process. The Federal Reserve Banks were exempted from the Government Corporation Control Act of 1945 in part because of the perception of private status. (See Chapter IV for an analysis of the accuracy of this perception.) 26/ Finally, the Federal Reserve System is often perceived to be a "profitmaker," given that it earns income and transfers its earnings (less expenses) to the Treasury. Federal Reserve System earnings are an outcome of the government's money-creation powers and have grown rapidly. Although any expenses of the Federal Reserve System decrease the net income of the Treasury, the growth in net income has dwarfed the growth in expenses. Therefore, some argue that increased Federal Reserve System spending may not be apparent (especially when excluded from the unified budget and when not subject to the appropriations process), and may create support for the budgetary independence of the Federal Reserve System among the beneficiaries of this spending. 27/

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26. Clifford, pp. 356, 390-91.

27. William F. Harrison, "The Relationship Between Federal Reserve Structure, Resource Allocation, and Political Independence," Social Science Quarterly, vol. 59 (September 1978), pp. 362-70.

CHAPTER III. AN OVERVIEW OF THE FEDERAL RESERVE SYSTEM

This chapter describes the current structure of the Federal Reserve System, its activities, and its financing methods and expenditures.

STRUCTURE

The Federal Reserve System consists of the Board of Governors, 12 Federal Reserve Banks, the Federal Open Market Committee, several other governing and advisory bodies, and member banks.

The Board of Governors. The Board of Governors has the responsibility to set System policy and support its operations. The seven Governors are appointed by the President and confirmed by the Senate. Governors serve for 14-year terms, with one term expiring every two years. The Chairman and Vice-Chairman are designated for four-year, renewable terms by the President and are confirmed by the Senate. The staff of the Board of Governors numbered 1,583 at the end of 1983.

The Federal Reserve Banks. The country is divided into 12 Federal Reserve Districts with a Reserve Bank in each District. Twenty-five branches and 11 regional check-processing centers have also been established. Each Bank has nine directors, six elected by member banks (three to represent the banking industry and three to represent business in general), and three appointed by the Board of Governors to represent the public, two of whom serve as chairman and vice chairman. Its president and first vice president are appointed by the directors, with the approval of the Board of Governors.

The Federal Reserve Banks employed 22,925 in 1983. Most Bank employees are involved in support and overhead activities (44 percent) and the provision of services to banks and the public (37 percent). Equal numbers (8 percent each) are engaged in supervision and regulation of banks and bank holding companies and in fiscal agent services for government agencies. Only 3 percent are directly involved in monetary and economic policy.

The Federal Open Market Committee. The Federal Open Market Committee (FOMC) is responsible for determining monetary policy and the course of open-market transactions. Open-market transactions are carried out by the managers for domestic operations and foreign operations of the

System Open Market Account, who are officers in the Federal Reserve Bank of New York. The FOMC consists of the seven Governors of the Board, and five Reserve Bank presidents. The president of the Federal Reserve Bank of New York is a permanent member; the other four Bank voting seats are rotated within groups of reserve districts. Non-voting presidents attend the meetings of the FOMC in Washington. The FOMC draws on the Board of Governors and Federal Reserve Banks for staff support.

Other Systemwide Bodies. The System has established three conferences of the chairmen, presidents, and vice presidents of the Banks. The latter two conferences contribute to Systemwide policymaking on operational matters. Systemwide staff level committees are used frequently to coordinate planning for the Banks.

Member Banks. All national banks are members of the Federal Reserve System. State-chartered commercial banks, trust companies, and mutual savings banks may join upon meeting the requirements of the System. At the end of June 1983, 5,758 banks were members of the Federal Reserve System. These banks were 39.7 percent of all insured banks, and held 73.[illegible] percent of insured banking assets.

ACTIVITIES

The activities of the Federal Reserve System can be generally categorized into four areas (called "service lines" by the Federal Reserve Banks): monetary and economic policy, services to the United States Treasury and government agencies, services to financial institutions and the public, and supervision and regulation of financial institutions. 1/

Monetary and Economic Policy

Monetary and economic policy activities are the most prominent functions performed by the System. The System attempts to promote price level stability and high levels of production and employment by influencing the

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1. Many of the activities of the Federal Reserve System are described in Board of Governors of the Federal Reserve System, The Federal Reserve System: Purposes and Functions, 6th ed. (1974). This publication (somewhat dated) emphasizes monetary policy. One chapter discusses the regulatory and supervisory functions. Coverage of services to the U.S. Treasury and other government agencies, and to financial institutions and the public, is sparse.

price of credit (interest rates) and the quantity of money (as measured by several money aggregates). The narrowest money aggregate, M1, consists of currency and demand deposits; M2 adds savings and small time deposits and general-purpose money market assets to M1; and M3 adds large time deposits and institutional money market assets to M2. 2/ The FOMC sets publicly announced target ranges of growth for these aggregates semiannually, and may revise the targets in light of changed economic conditions.

The primary tool of monetary policy is the sale and purchase of U.S. government securities in the open market. Open-market operations, carried out by the Federal Reserve Bank of New York, allow the Federal Reserve System to control indirectly interest rates or the rate of growth of money. Two other monetary policy instruments are available to the Federal Reserve System: reserve requirements and the discount window. Reserve requirements specify the minimum quantity of reserves (vault cash and deposits with the Federal Reserve Banks) that depository institutions must hold against certain types of deposits. 3/ If, for example, a bank's required reserve ratio against demand deposits is 12 percent, it is required to hold 12 cents in reserve assets for each dollar in demand accounts. Within limits specified by law, the Federal Reserve System may define reserve assets and change reserve ratios, thus changing the maximum volume of deposits subject to requirements. Depository institutions may borrow reserves from the Federal Reserve Banks at the System's discount rate or from the excess reserves of other institutions in the federal funds market.

The open-market operations of the Federal Reserve affect the supply of money by changing the supply of bank reserves. Assume, for example, that the reserve ratio is set at 12 percent and that the banking system is just meeting the required reserve ratio. If the Federal Reserve System purchased $1 billion in government securities in the open market, it would present the sellers of these securities with checks drawn on itself. The sellers would deposit these checks in their banks, the banks would present the checks to the Federal Reserve Banks, and the Federal Reserve Banks would pay these banks by crediting the banks' accounts at the Federal

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2. Technical definitions of money aggregates are available in the 1983 Annual Report of the Board of Governors, p. 16.

3. Until 1980, only member banks were subject to reserve requirements. Nonmember banks and thrift institutions also became subject to reserve requirements on a phased-in basis after passage of the Monetary Control Act of 1980.

Reserve System. 4/ Because deposits with the Federal Reserve count as reserves, total reserves would thereby be increased by $1 billion. With $1 billion in additional reserves, the banking system could at most increase deposits by $8.3 billion (additional reserves divided by the reserve ratio of 12 percent) by making loans or buying securities. Either would have the effect of putting downward pressure on short-term interest rates. Conversely, a sale of securities by the System reduces reserves and causes a constriction of the quantity of money, and may result in upward pressure on short-term interest rates. Most trading is meant to offset technical, temporary changes in reserves (such as unexpected Federal Reserve check collection float caused by transportation problems) or to compensate for uncertainty about the trend in reserve balances. Such factors, along with changes in bank holdings of excess reserves or the public's desire for currency, prevent the Federal Reserve from having precise control over the money supply in the very short run. In the longer run it can, if it desires, generally approximate its money supply targets. Temporary adjustments are made through repurchase agreements (which supply reserves) and matched sale-purchase transactions (also known as "reverse repurchase agreements," which subtract reserves). Daily security transactions range in size from several hundred million to several billion dollars.

A depository institution may borrow funds from its Federal Reserve Bank (with the Bank's permission) at the discount "window" by receiving an advance on acceptable assets (mostly government securities). 5/ The discount window is used by depository institutions to cover unexpected deposit or portfolio changes. It is also intended to serve as a reliable source of liquidity if financial markets are in disarray--the "lender of last resort" function. Use of the discount window increases the reserves of depository institutions. Discount rates are determined by the System and may be set in coordination with open-market policy and in light of the cost to depository institutions of funds from alternative sources. Rates may vary by the term of the extension. At the end of 1983, loans and acceptances outstanding totalled $1.3 billion.

The Federal Reserve participates in the international financial system through the Federal Reserve Bank of New York under the direction of the FOMC. The Bank may buy and sell currencies to moderate movements in

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4. These transactions are actually carried out by wire transfers.

5. A common request from visitors at Federal Reserve Banks is to see the discount window. The term refers to a borrowing arrangement, which does not have a genuine teller station counterpart.

the foreign exchange value of the dollar. It handles transactions with foreign central banks who wish to sell or buy Treasury securities. The Federal Reserve Bank of New York also holds the international reserve assets of the Treasury Department's Exchange Stabilization Fund. The international transactions of the Federal Reserve are buttressed by special regulations on banks and holding companies engaged in foreign banking. These regulations establish special reserve requirements and limitations on foreign lending volumes.

The Federal Reserve System also has considerable regulatory power over credit flows, based on numerous banking and securities laws. These controls have had various purposes—preventing rapid growth in credit extensions, maintaining stability in financial markets, ensuring the soundness of the banking system, and allocating credit to specific purposes. For example, Regulations G, T, U, and X limit the amount of credit available for the purchase of securities. These "margin requirements" stipulate that a percentage of a stock or security purchase must be collateralized (currently 50 percent in most instances).

Services to the U.S. Treasury and Government Agencies

The Federal Reserve Act designates the Federal Reserve Banks as fiscal agents for the United States government. Under the general supervision of the Treasury, the System maintains the Treasury Tax and Loan and other transactions accounts (over 10.4 million transactions in 1983). The System issues (sells), reissues and replaces, services, and redeems savings bonds, other Treasury securities, and the securities of other government agencies. It also redeems and ultimately destroys food stamps for the Department of Agriculture, processing 2.7 billion coupons in 1983.

Services to Financial Institutions and the Public

The Federal Reserve System is a major participant in the payments system. It provides coin and currency distribution, check processing and collection, wire transfer and settlement services, automated clearinghouse services, and safekeeping, book-entry, and coupon collection for securities. The System also provides informational benefits to its members and the public.

In the currency and coin services, the Federal Reserve Banks process and wrap, distribute, and verify Federal Reserve notes and coin. In 1983, for example, the Banks processed $9.7 billion in worn notes and counterfeit currency, destroying $3.9 billion of it. They shipped 8.6 million containers of currency and coin, using armored carriers that made over 550,000 stops. New coin and currency are purchased from the Bureau of the Mint and the Bureau of Engraving and Printing.

Check collection is the major activity in this service line. Checks are received from depositing institutions, processed through check-sorting machines at Federal Reserve Banks and regional check processing centers, transported across the country, and presented to paying institutions. Uncollected checks ("return items") are sent back to depositing institutions. The Banks directly participated in the collection of over 14.9 billion commercial and U.S. government checks in 1983. This was approximately 36 percent of the total checks written.

The Federal Reserve Banks aid collection of many of the checks they do not process directly by providing wire transfer and settlement services to banks and check clearinghouses. Institutions often present checks directly to each other and indirectly through correspondent banks and check clearinghouses. Institutions may settle their obligations from these exchanges by making adjustments in their clearing and reserve account balances at the Federal Reserve Banks. Settlement is made through the "Fedwire," an electronic communications system that is also used to transfer reserves in the federal funds market.

Rapid growth in the numbers of checks presented for collection has led to increased costs to the banking sector. In response, the Federal Reserve Banks have made an effort to replace paper checks with electronic funds transfers, especially through the development of automated clearinghouses (ACH). ACH facilities process computer tapes with bulk payments, such as payrolls and dividends. In 1983, 156.5 million commercial items and 240.3 million government items were processed using automated clearinghouse operations, servicing nearly 30,000 financial institutions.

In their security safekeeping activities, the Federal Reserve Banks hold government securities in both definitive and book-entry form. Transfers of ownership of Treasury securities are accomplished through computerized book-entry form, which reduces the need for hard copies. Non-cash items such as coupons on state government bonds are collected and presented to paying agents. Finally, Federal Reserve Banks and the Board of Governors perform a variety of informational services for banks and the public, including publications, seminars, data dissemination, and cost-accounting assistance for small banks.

Supervision and Regulation of Financial Institutions

The Federal Reserve System plays a major role in the supervision and regulation of banks. Its activities are based on powers granted in the Federal Reserve Act, the Banking Acts of 1933 and 1935, the Bank Holding Company Act of 1956 (and amendments of 1966 and 1970), the Bank Merger Act of 1960, and many other banking laws.

The general purpose of these laws is to further the safety and soundness of the banking system. The laws limit the permissible commercial activities of banks and their holding companies and the permissible banking activities of commercial corporations. Concentration in the banking industry is restricted by limitations on interstate banking and by necessary approval for bank acquisitions and mergers. 6/ Banking laws also empower the bank regulatory agencies to conduct regular examinations and require periodic reports to ensure adequate capitalization, competent management, and prudent loan portfolios.

The System shares regulatory jurisdiction over commercial banks at the federal level with the Comptroller of the Currency and the Federal Deposit Insurance Corporation (state banking agencies may also regulate banks with state charters). Operational responsibilities (for examinations, for example) are divided by law and by practice among these agencies. The Federal Reserve System is primarily responsible for examination of state-chartered member banks, whereas the Comptroller oversees national member banks and the FDIC oversees non-member insured banks. These agencies along with the Federal Home Loan Bank Board and the National Credit Union Administration comprise the Federal Financial Institutions Examination Council, a coordinating body. The Federal Reserve System also oversees bank holding companies, U.S. corporations involved in international banking and trade, and certain foreign bank operations in the United States. 7/

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6. Commercial corporations and banks have aggressively sought and exploited loopholes in these laws in recent years. The creation of "nonbank banks" and the nearly nationwide activities of certain banks has led to active consideration of banking regulation bills by the Congress. See F. Jean Wells, "Financial Deregulation: Current Status and Legislative Issues," Congressional Research Service (1984).

7. See Andrew S. Carron, "Banking on Change: The Reorganization of Financial Regulation," The Brookings Review (Spring 1984), pp. 12-21.

Supervisory and regulatory activities are carried out by both the Board and the Federal Reserve Banks. The Board is responsible for setting policy, and the Banks conduct examinations. Major activities in this service line include examinations of state member banks (736 in 1983), inspections of bank holding companies and their non-bank subsidiaries (1,398 in 1983) and reviews of bank holding company applications (2,542 in 1983). The System also reviews mergers, bank acquisitions, and changes in bank control. Periodic reports on the condition and income of banks and holding companies are collected, processed, and made available to the public. International activities include monitoring the international debt exposure of banks and the debt service capabilities of borrowing countries.

In the consumer protection and credit availability areas, the Federal Reserve System is responsible for adopting regulations for all financial institutions and for enforcing regulations for state member banks. Laws in the System's jurisdiction include the Truth in Lending Act, the Equal Credit Opportunity Act, the Electronic Fund Transfer Act, the Home Mortgage Disclosure Act, and the Community Reinvestment Act. 8/

FINANCING AND EXPENDITURES

During calendar year 1983, the Federal Reserve contributed $14.2 billion of earnings to the revenues of the Treasury Department. Federal Reserve earnings are net of the expenses of the Federal Reserve Banks and Board, dividends to member banks, and other deductions. In 1983, deductions included $1,100.2 million in operating expenses for the Federal Reserve Banks, $70.4 million in Board expenses, and $85.2 million in dividends to member banks. 9/ These deductions reduced the amount of Federal Reserve earnings available to the Treasury to finance other government operations.

Description of the financing and expenditures of the Federal Reserve System is complicated by the decentralized structure of the System. Separate balance sheets and operating statements are prepared for the 12

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8. The Supervision and Regulation service line also includes monitoring of reserve accounts and formulation of margin requirement and interest rate ceiling regulations mentioned above under Monetary and Economic Policy.

9. All figures are for calendar years.

Banks, the Banks as a whole, and the Board, and are presented in the Annual Report of the Board of Governors. Because the Banks and the Board budget separately and use different accounting concepts, their financing and expenditures are discussed separately in this report.

Federal Reserve Banks

The Federal Reserve Banks earn almost all of the income of the Federal Reserve System, and incur approximately 95 percent of its expenses. Table 1 shows the income, expenses, and net earnings of the Banks for calendar year 1983.

About 94 percent of Federal Reserve Banks' earnings are interest payments on U.S. government securities. The amount of interest earnings is a function of interest rates on government securities and the size and maturity distribution of the portfolio. Other earnings related to monetary policy are interest on Federal Reserve advances and discounts (0.9 percent) and on foreign currencies (1.7 percent). Service fees from depository institutions and the public (3.1 percent) constitute the remainder.

The money-creation powers of the Federal Reserve System ensure that the System will be profitable. As sole holder of the right to issue currency whose cost of production is a fraction of its value in exchange, the Federal Reserve System captures the "seigniorage" in the money creation process. Like monarchs of old, the Federal Reserve makes money by making money. It does this first by purchasing Federal Reserve Notes at the cost of production (less than 3 cents per note) and by issuing the notes at par. These non-interest bearing IOUs (Federal Reserve Notes) are then exchanged for interest bearing assets (government securities). Securities are also purchased with the funds on deposit in Reserve Banks that meet reserve requirements and serve as clearing balances (these accounts are also the means by which currency is exchanged for securities). These securities are added to the System's portfolio, and the interest income from the securities is used to fund expenses or is returned to the Treasury. Table 2, the Statement of Condition (balance sheet) of the Federal Reserve Banks, shows the Federal Reserve Note liabilities and government security assets of the Banks at the end of 1983. 10/

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10. The potential earnings of the System from money creation are limited by the goal of price level stability. Securities purchases increase reserves and the money supply.

TABLE 1. INCOME, EXPENSES, AND EARNINGS OF THE FEDERAL RESERVE BANKS, 1983 (In millions of dollars)

Income a/		Expenses a/	
Interest on U.S. Government Securities	15,150.2	Salaries and Other Personnel Expenses	499.6
Interest on Discounts	138.9	Retirement and Other Benefits	141.2
Interest on Foreign Currencies	273.8	Postage and Shipping	97.1
Priced Services Fees	496.2	Equipment	114.7
Other	9.3	Buildings	82.4
		Earnings Credits	71.8
Current Income	16,068.3	Recoveries and Capitalized Expenses	-17.2
		Other	116.7
		Current Expenses	1,100.2 b/
		Reimbursements	-76.6
		Net Current Expenses	1,023.7

Current Net Income	15,044.7
Adjustments	-400.4
Adjusted Net Income	14,644.3

Distribution of Adjusted Net Income	
Cost of Currency Assessment	152.1
Board of Governors Expenses Assessment	71.6
Dividends	85.2
Transfer to Surplus	106.7
Payment to U.S. Treasury	14,228.6

SOURCE: Board of Governors of the Federal Reserve System, Annual Report (1983), Table 7.

a. Details may not add to totals because of rounding.

b. Total expenses are $5.9 million less than the sum of expense categories because of a deduction of Federal Reserve Communications System expenses in the Federal Reserve Bank of Richmond's account.

ADDENDUM: The display of Federal Reserve Bank income and expenses may be recast to show income and expenses on a grossed-up basis. This recasting would shift recoveries ($14.6 million) and reimbursements to the income accounts and shift the cost of currency production to the expense accounts, showing gross current income as $16,159.5 million and gross current expenses as $1,266.9 million.

TABLE 2. STATEMENT OF CONDITION, FEDERAL RESERVE BANKS, December 31, 1983 (In millions of dollars)

Assets		Liabilities	
U.S. Government and Agency Securities	160,795.0	Federal Reserve Notes	157,098.6
Loans and Acceptances	1,335.7	Deposits	26,126.1
Gold and SDR Certificates, and Coin	16,155.1	Deferred Availability Cash Items	9,958.2
Cash Items in Process of Collection	11,564.3	Other Liabilities	2,464.0
Bank Premises and Other Assets	8,724.8	Total Liabilities	195,646.9
Total Assets	198,575.1	Capital, Paid-in	1,464.1
		Surplus	1,464.1
		Total Liabilities and Capital Accounts	198,575.1

SOURCE: Board of Governors of the Federal Reserve System, Annual Report (1983), Table 1.

The expenses of the Federal Reserve Banks (see Table 1) are largely for personnel, as the operations of the System are labor-intensive. In 1983, salaries and other personnel expenses cost $499.6 million, and retirement and other benefits another $141.2 million. Equipment expenses were $114.7 million and building expenses were $82.4 million. Postage and shipping costs, mostly for the transportation of checks and currency, were $97.1 million. The cost of earnings credits—interest on clearing balances of the banks that participate in the payments system—amounted to $71.8 million, and $116.7 million went to other expenses such as travel and communications. The Banks received $14.6 million in recoveries and temporarily capitalized $2.6 million of expenses. Reimbursements from government agencies for fiscal agent activities are subtracted to obtain net current expenses.

Subtracting net current expenses from current income yields current net income in the amount of $15,044.7 million in 1983. The Federal Reserve Banks made adjustments to net income of -$400.4 million in 1983, primarily adding profits on sales of securities and subtracting unrealized losses on foreign currency holdings. The resultant adjusted net income was reduced by four amounts:

- The cost of currency production: $152.1 million. This is the amount of reimbursement for production costs paid by the Federal Reserve Banks to the Bureau of Engraving and Printing through the Board of Governors. 11/

- Payments of semiannual assessments for Board of Governors expenses—$71.6 million;

- Annual dividends to member banks at the rate of 6 percent on their capital subscriptions—$85.2 million; and

- A transfer to the Federal Reserve Banks' surplus to bring it level to the amount of paid-in capital from member banks—$106.7 million.

The remaining net income is paid to the Treasury in amounts transferred weekly.

Building and equipment expenses of the Federal Reserve Banks are unusual compared to other federal agencies. The Federal Reserve Banks paid $19.4 million in real estate taxes in 1983, as required by the Federal Reserve Act; other federal agencies do not pay real estate taxes but may make payments in lieu of taxes to certain jurisdictions. Second, the Federal Reserve Banks charge depreciation as an operating expense instead of following the practice of other federal agencies (including the Board of

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11. The cost of currency production is also carried in the Board of Governors' budget, but in the amount of $128.2 million in 1983. This is the actual amount spent on currency by the System in 1983. The additional $23.9 million (resulting in the total of $152.1 million) is a single-year amortization of previous-year currency costs made necessary by the change in the accounting treatment of currency from an expense in 1982 to an assessment in 1983.

Governors) of charging the entire purchase price in the year of acquisition. 12/ Building depreciation was $18.9 million in 1983 and equipment depreciation was $39.7 million. Remaining expenses in the buildings and equipment categories were utilities, rent, and repairs and maintenance.

Actual capital outlays of the Federal Reserve Banks are shown in Table 3. The annual report of the Board of Governors does not include a record of these outlays. The level of total Federal Reserve Bank outlays can be found by adding the amount of capital outlays to total expenses less depreciation charges. The results, shown in Table 4, increase the reported expenditures of the Banks by 3.5 percent.

TABLE 3. FEDERAL RESERVE BANKS' CAPITAL OUTLAYS, 1983
(In millions of dollars)

Data Processing and Communications Equipment	52.1
Furniture and Furnishings	6.5
Other Equipment	14.9
Land	0.5
Buildings	18.5
Building Machinery	4.6
Leasehold Improvements	0.3
Total	97.2a/

SOURCE: Capital outlays data supplied by the Board of Governors of the Federal Reserve System.

a. Details do not add to total because of rounding.

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12. The Banks use straight-line historical cost depreciation, capitalizing expenditures on most physical assets with useful lives of beyond a year. The Postal Service also capitalizes and depreciates its major capital purchases. Some federal agencies pay "Standard Level User Charges" (SLUCs). SLUCs are rent-like fees for building occupancy.

TABLE 4. FEDERAL RESERVE BANKS' TOTAL OUTLAYS, 1983
(In millions of dollars)

Current Expenses	1,100.2
Less depreciation	-58.6
Current Outlays	1,041.6
Capital Outlays	97.2
Total Outlays	1,138.8

SOURCE: Board of Governors of the Federal Reserve System, Annual Report (1983), Table 7; capital outlays data supplied by Board of Governors.

Table 5 shows the composition of Federal Reserve Bank's expenses by service line. Almost two-thirds of the expenses of the Banks are in the Services to Financial Institutions and the Public service line. Spending in the other three service lines is in roughly equal amounts. These spending data are drawn from the Planning and Control System (PACS) of the Federal Reserve System, which allocates costs among services (for example, "adminstration of laws and regulations related to banking" in the Supervision and Regulation service line) and activities ("processing holding company applications" in the same service). This system also records indirect costs for support and overhead activities that are then allocated to the four service lines. Major support services include data communications ($39.6 million), data processing ($93.5 million), data systems support ($93.9 million), and building operations ($104.9 million). Support services constitute 30.3 percent of total direct and indirect expenses (that is, before support and overhead costs are allocated to service lines). Overhead services (administration, budgeting and accounting, personnel, systemwide projects, etc.) are 33.5 percent of total direct and indirect expenses.

Table 6 shows Federal Reserve Bank expenses before and after reimbursements and collections. Most reimbursements are for fiscal agent services from the Treasury and Department of Agriculture. All collections are from priced services fees.

TABLE 5. COMPOSITION OF FEDERAL RESERVE BANKS' CURRENT DIRECT AND INDIRECT EXPENSES, 1983
(In millions of dollars)

		Total Expenses	Percent of Total Expenses After Reallocation
A.	Monetary and Economic Policy	100.4	9.8
	Services to U.S. Treasury and Government Agencies	120.3	11.7
	Services to Financial Institutions and the Public	675.9	65.7
	Supervision and Regulation	131.8	12.8
	Total expenses	1,028.5	

		Indirect Expenses	Percent of Total Expenses Before Reallocation
B.	Support	312.1	30.3
	Overhead	344.3	33.5

SOURCES: Board of Governors of the Federal Reserve System, Planning and Control System (PACS) Expense Report, 1983; and Board of Governors staff.

Notes: Part A shows expenses for output service lines, with support and overhead expenses allocated to the service lines. Part B shows indirect expenses before allocations as a percent of direct and indirect expenses. PACS includes all current expenses in Table 1 except for the cost of earnings credits--the cause of the difference between total expenses here and in Table 1. Because capital outlays are not allocated to service lines by the Federal Reserve Banks, all tables using PACS data report capital spending as represented by depreciation charges.

TABLE 6. COMPOSITION OF FEDERAL RESERVE BANKS' CURRENT EXPENSES, NET OF REIMBURSEMENTS AND COLLECTIONS, 1983 (In millions of dollars)

	Current Expenses				Net Expenses	
	Millions of Dollars	Percent	Reimbursements	Collections	Millions of Dollars	Percent
Monetary and Economic Policy	100.4	9.8	0.5	0.0	99.9	21.9
Services to U.S. Treasury and Government Agencies	120.3	11.7	72.9	0.0	47.4	10.4
Services to Financial Institutions and the Public	675.9	65.7	3.0	496.2	176.7	38.8
Supervision and Regulation	131.8	12.8	*	0.0	131.8	28.9
Total	1,028.5	100.0	76.4a/	496.2	455.8	100.0

SOURCES: Board of Governors of the Federal Reserve System, Planning and Control System (PACS) Expense Report, 1983; and Board of Governors staff.

* Less than $50,000.

a. The $149,658 disparity between Table 2 reimbursements and PACS-reported reimbursements is due to a currently unrectified reporting error in PACS.

NOTES: Current expenses are net of recoveries ($14.6 million). All support and overhead costs are allocated to output service lines. As Table 5 does not show $71.8 million in earnings credits costs as expenses, Table 6 does not show $84.9 million in income from clearing balances. Details do not add because of rounding.

Board of Governors

Table 7 shows the income and expenses of the Board of Governors. Ninety-eight percent of income is from assessments on the Federal Reserve Banks. Most publications revenue is from the Federal Reserve Regulatory Service, which provides information on regulatory actions. Net revenue

TABLE 7. INCOME AND EXPENSES OF THE BOARD OF GOVERNORS, 1983 (In millions of dollars)

Income	
Assessments on Federal Reserve Banks	71.6
Sale of Publications	1.1
Other	0.5
Total	73.1 a/
Expenses	
Salaries	47.1
Retirement and Insurance Contributions	7.7
Buildings and Equipment	4.7
Communications	3.7
Travel	1.9
Contractual Services	2.0
Other	3.3
Total	70.4
Net Income	2.7
Adjustment for unfunded accrued annual leave	-0.3
Net Revenue	2.4 b/

SOURCE: Board of Governors of the Federal Reserve System, Annual Report (1983), p. 208.

a. Details may not add to total because of rounding.

b. A Federal Reserve payment of $128.2 million to the Treasury for currency production was offset by reimbursement from the Federal Reserve Banks.

(after an adjustment for unfunded annual leave) was $2.4 million. The Board of Governors had a cash balance of $5.8 million and total assets of $85.8 million (including $61.2 million in buildings valued at cost) at the end of 1983.

Like the Federal Reserve Banks, expenses are largely for personnel--66.8 percent in salaries and 10.9 percent in retirement and other benefits. Building and equipment expenses include utilities, repairs and maintenance, equipment purchases, rentals, and property additions. Buildings and equipment expenses for 1983 are low relative to previous years, when the two Board of Governors buildings were undergoing construction and renovation and when computers were acquired.

TABLE 8. COMPOSITION OF BOARD OF GOVERNORS' EXPENSES, 1983
(In millions of dollars)

Expenses	
Formulation of Monetary Policy	16.1
Supervision and Regulation of Financial Institutions	15.4
Financial Services for System, Government, and Public	0.7
System Policy Direction and Support	38.5
Total	70.7
Offsetting Collections	
Federal Funds	0.1
Non-federal Funds	73.0
Total	73.1

SOURCE: Board of Governors staff.

NOTE: Expenses include $0.3 million in unfunded accrued annual leave distributed to programs.

Table 8 shows the composition of Board of Governors expenses in the Program and Financing format used in the Budget Appendix. This categorization of Board of Governors expenses is produced only for the Budget Appendix and is not based on the regular accounting procedures of the Board, which are structured by office and division. The first program category is similar to the Federal Reserve Bank service line for Monetary and Economic Policy. The Supervision and Regulation program category contains the expenses of supervision and regulation of member banks, bank holding companies, and supervision of Reserve Banks. The expenses shown in the Financial Services category are restricted to those for service pricing and systemization of automation. The fourth program activity of the Board of Governors, "system policy direction and support," represents all policymaking, overhead, and support activities. These activities are not reallocated to output activities as they are by the Federal Reserve Banks' Planning and Control System. When major capital outlays are made, these outlays are reported in a separate line in the Budget Appendix.

CHAPTER IV. BUDGET PRESENTATION OF THE FEDERAL RESERVE

Every January the President sends the Congress his proposed budget for the next fiscal year. The budget provides comprehensive information about the financial operations of government agencies. It also shows the President's recommended fiscal policy, includes the Administration's requests for budget-related legislation, and indicates the probable financing needs of the Treasury for the upcoming year.

The budget provides only limited information on the Federal Reserve System. The data are adequate for the purpose of projecting Treasury financing needs, since they include an estimate of the Federal Reserve System's transfer of earnings to the Treasury. They are inadequate, however, to the extent that the budget is to inform the Congress and the public of the proposed allocation of the government's limited financial resources. Almost all Federal Reserve System operating expenses are currently excluded from the budget.

The purpose of this chapter is to explore the feasibility of a complete presentation of Federal Reserve finances in the budget documents. The chapter begins by describing the System's current budget presentation and the reasons why it is so limited. The chapter then considers whether the Federal Reserve's finances are compatible with the budget concepts used to describe the finances of other federal agencies. It concludes by discussing whether Federal Reserve financial operations can be accurately estimated in advance, and whether the Federal Reserve's independence would be seriously weakened by requiring a complete budget presentation. 1/

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1. The latter issue was underscored recently in the report of the Task Force on the Budget Process of the House Committee on Rules, which included the following: "To the degree that the U.S. Postal Service and the Board of Governors of the Federal Reserve System are independent establishments, the Task Force believes these entities should continue to be excluded from the unified budget." House Committee on Rules, Report of the Task Force on the Budget Process (May 1984), p. 43. The budgetary status of the Federal Reserve was also studied by the House Budget Committee in 1976, which reported, "It is the Committee's view that the expenses and budget status of the Board should be considered at a later time." Off-Budget Activities of the Federal Government, H.Rept. 94-1740 (September 30, 1976), p. 4.

LIMITATIONS OF THE CURRENT BUDGET PRESENTATION

The U.S. government's budget documents routinely include certain types of information about the financial operations of government agencies and programs. Finances are summarized in the main budget document and presented in detail in the Appendix volume. The Budget Appendix contains at least two financial schedules for all programs--for Program and Financing and for Object Classification. A Program and Financing Statement lists the major categories of program activity giving rise to a flow of obligations, and the flow of financing for the discharge of these obligations. An Object Classification Schedule describes the types of goods and services to be purchased (salaries, travel, printing, for example) regardless of the program purpose being served. Specialized schedules may also be included for certain programs. For example, a Statement of Financial Condition (or balance sheet) shows the assets, liabilities, and equity of a government corporation, and a Status of Direct Loans statement shows the volume of direct loan originations and repayments.

The complex finances of the Federal Reserve (see the box on the following page) are not included in the main budget document except for a single entry for the Federal Reserve earnings that are transferred to the Treasury. This transfer is classified as a "miscellaneous receipt" on the revenue side of the budget, as shown in Table 9. The earnings consist of gross income minus operating expenses, dividends, and other adjustments. The Appendix volume includes schedules of Program and Financing, Object Classification, and Financial Condition for the Board of Governors, but no information on Federal Reserve Bank operating expenses is presented anywhere in the budget documents. The Board of Governors is shown in the Appendix as an off-budget federal entity, but is not included in the tabulation of off-budget outlays. Its budget is presented on a calendar year basis, and covers only a quarter of the federal budget year. The fiscal year 1985 Appendix, which was published in early 1984, included estimates of Board of Governors spending through December 1984 and estimates of federal agency spending through September 1985. Table 10 shows the Program and Financing schedule of the Board of Governors for fiscal year 1985.

Current presentation thus limits the amount of public information on Federal Reserve finances that is comparable to readily available information on the finances of other government agencies. It might be argued that these data are already available in the Annual Report of the Board of Governors, but that report receives much less public attention than do the budget documents. Moreover, it does not show some information that the Appendix, other agency reports, and justification books for appropriations requests routinely provide. For example, it does not include data on current Federal Reserve Bank outlays for capital purchases. Ordinarily, users of

Federal Reserve Financial Operations

The Federal Reserve Banks buy, through the Board of Governors, Federal Reserve Notes from the Bureau of Engraving and Printing at the cost of production. The notes are sold to depository institutions by means of reserve accounts, which most depository institutions must keep with the Federal Reserve Banks.

The Federal Reserve Banks own and trade government securities and foreign currency for the purpose of conducting monetary policy. Unrealized capital gains and losses result when the market values of the securities and foreign currency fluctuate. Realized capital gains and losses result when the Banks sell securities and foreign currency.

The Federal Reserve Banks make interest-earning loans to financial institutions through the discount window. These loans return income at the discount rate, which is usually below the earnings rate on the Federal Reserve Banks' portfolios.

The Federal Reserve Banks transfer checks and securities across the country, often crediting the accounts of depositing institutions before collecting from paying institutions--resulting in a "float." The cost of float is recovered from depository institutions.

The Federal Reserve Banks and the Board of Governors spend cash for operating expenses--salaries, retirement, buildings, equipment, shipping, etc. The Banks also receive collections from the private sector in return for financial services, and reimbursements from government agencies for fiscal agent services.

The Federal Reserve Banks finance the expenses of the Board of Governors by paying assessment charges to the Board. They also pay member banks annual dividends on their capital subscriptions and transfer capital to the Banks' surplus accounts.

The Federal Reserve Banks transfer their current income net of expenses, assessments, dividends, adjustments, and additions to surplus to the Treasury. Most of the income is derived from payments by the Treasury on its securities held by the Federal Reserve.

TABLE 9. FEDERAL RESERVE BUDGET PRESENTATION FOR FISCAL YEAR 1985: TOTAL BUDGET RECEIPTS
(In millions of dollars)

Source	1983 Actual	1984 Estimate	1985 Estimate
Individual Income	288,938	293,260	328,410
Corporation Income	37,022	66,606	76,540
Social Insurance	208,994	239,494	270,683
Excise, Estate, Gift and Custom	50,008	53,181	53,458
Miscellaneous			
Deposit of earnings, Federal Reserve System	14,492	14,352	14,799
All other	1,109	3,179	1,238
Total Budget Receipts	600,562	670,071	745,127

SOURCE: Executive Office of the President, The Budget of the United States Government, Fiscal Year 1985.

capital budgets show in a supplementary statement the sources and uses of funds for capital acquisitions. The Annual Report does not include such a statement, as the Federal Reserve Banks do not need to go to the market to fund capital purchases. A capital purchase is represented only by an increase in the value of building or furniture and equipment assets included in the Statement of Condition, but this amount may be offset by depreciation charges for existing capital assets or by disposal of assets. Furthermore, the Annual Report does not display Federal Reserve Bank administrative expenses by program, nor does it project future expenses. Separate books and accounting practices for the Board of Governors and the Federal Reserve Banks also prevent easy calculation of totals for Systemwide spending by program.

Even the limited information currently included in the Budget Appendix—on the expenses of the Board of Governors--is not timely. The figure for the Federal Reserve deposit of earnings is reached by netting of

TABLE 10. FEDERAL RESERVE BUDGET PRESENTATION FOR FISCAL YEAR 1985: BUDGET APPENDIX PROGRAM AND FINANCING SCHEDULE
(In thousands of dollars)

	Calendar Year		
Board of Governors	1982 Actual	1983 Estimate	1984 Estimate
Program by Activities			
Operating Expenses			
Formulation of monetary policy	15,163	15,289	16,717
Supervision and regulation of financial institutions	13,728	15,751	16,145
Financial services for system, government and public	886	701	880
System policy direction and support	35,524	38,027	40,797
Total operating expenses	65,301	70,768	74,539
Capital Investment			
Computer acquisition	900	---	---
Total program costs	66,201	70,768	74,539
Changes in selected resources	17	---	---
Total obligations	66,218	70,768	74,539
Financing			
Offsetting collections from:			
Federal funds	-123	-122	-122
Non-federal sources	-61,813	-71,551	-72,600
Unobligated balance available, start of year	-582	3,700	2,795
Unobligated balance available, end of year	-3,700	-2,795	-4,612
Budget Authority	---	---	---
Relation of Obligations to Outlays:			
Obligations incurred, net	4,282	-905	1,817
Obligated balance, start of year	5,583	8,314	6,937
Obligated balance, end of year	-8,314	-6,937	-7,114
Outlays	1,551	472	1,640

SOURCE: Executive Office of the President, The Budget of the United States Government, Fiscal Year 1985.

Federal Reserve income and expenses. This failure to show Federal Reserve Bank expenses explicitly leads to underreporting of the total program obligations of the federal government; thus governmentwide administrative expenses for financial regulation, economic policy, and debt marketing are actually higher than shown in the budget documents. The large volume of Federal Reserve business-type activities (for example, check collection) are also obscured from public view.

REASONS FOR THE CURRENT BUDGET PRESENTATION

The incomplete presentation of Federal Reserve finances in the budget is not the result of any legislation explicitly directing that the Federal Reserve be excluded from the budget documents. Rather, the most important reason for the Federal Reserve's current budget presentation is the 1967 recommendation of the President's Commission on Budget Concepts. It has also been suggested that the quasi-private status of the Federal Reserve Banks bars including their finances in the budget. These causes are discussed in turn.

The President's Commission on Budget Concepts

Until fiscal year 1969, the budget documents simultaneously reported two different budgets:

- The administrative budget, which was limited to federal funds in the General Fund of the Treasury; and
- The consolidated cash budget, which included both federal and trust funds.

Federal Reserve net income was included in both the administrative and consolidated cash budgets as miscellaneous receipts. The different coverages of these budgets created problems. Although the President's budget documents usually centered on the administrative budget (the budget that was limited generally to appropriated accounts), this budget included only about 75 percent of the government's financial activities. Many budgetary experts believed that the lack of coverage of trust funds allowed trust fund programs to grow rapidly without sufficient Congressional review. Additionally, the existence of two budgets meant two different deficits, which led to a great deal of confusion among the public. Administrations occasionally publicized the consolidated cash budget more heavily if it showed a smaller deficit than did the administrative budget.

Responding to these problems, the Commission on Budget Concepts recommended that the federal government report its revenues and expenditures in a single "unified budget." Central to the unified budget concept was the comprehensiveness of its coverage:

> . . . different and competing budgets confuse public and congressional understanding and impede governmental decision-making . . .
>
> The Commission's major recommendations with respect to coverage of the budget are:
>
> o The budget should, as a general rule, be comprehensive of the full range of Federal activities. Borderline agencies and transactions should be included in the budget unless there are exceptionally persuasive reasons for exclusion. Specifically, the budget should include the transactions of the Federal trust funds which are now outside the administrative budget (although the Commission believes that the identity and integrity of trust funds should be maintained);
>
> o Most agencies and transactions now included in the consolidated cash budget should continue to be reflected in the budget. However, the Commission recommends exclusion from the budget of those Governmental-sponsored activities which are now completely privately owned, and local receipts and expenditures of the District of Columbia Government; 2/

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2. Report of the President's Commission on Budget Concepts, Government Printing Office (1967), pp. 2, 25. Support for the concept of a unified budget has remained strong. A recent report of the Committee on Economic Development, for example, stated: "We strongly believe that continued adherence to a comprehensive, unified budget is essential to the effectiveness and credibility of the budget process. A unified budget that includes all activities by federally owned entities is necessary to allow the Executive and Congress to make informed decisions on the overall fiscal and financial impact of federally owned activities and to serve as a framework for trade-offs among competing claims on federal fiscal resources. Crosscuts of budgetary information should be complementary to the unified budget, not a substitute for it." Committee on Economic Development, Strengthening the Federal Budget Process: A Requirement for Effective Fiscal Control (June 1983), p. 27.

The Commission found, however, some persuasive reasons for exclusion of the Federal Reserve System from the unified budget:

> The Federal Reserve System is a government instrumentality which Congress has established principally to execute its responsibilities with regard to the Nation's money supply.
>
> The Federal Reserve System is responsible to the Congress, and reports annually to the Congress on the results of its operations. Discussions about the independence of the Federal Reserve System are concerned with its position within the Federal Government—not whether it is independent of the Federal Government. The System is clearly a Federal Government Operation.
>
> Each of the three present budget concepts includes as a receipt the payment to the Treasury of excess Federal Reserve profits. Apart from this receipt, none of the three budgets includes receipts and expenditures of the Federal Reserve System arising from its lending and other activities. Inclusion of the Federal Reserve banks in the Federal budget might jeopardize the vital flexibility and independence of the monetary authorities. Moreover, projections of System operations for a forward period—as would be required if included in the budget—do not appear feasible at the present time. The nature and economic significance of Federal Reserve bank "receipts" and "expenditures" are different from those of most other government programs and activities.
>
> For the above reasons the Commission recommends:
>
> The payment of excess Federal Reserve profits to the Treasury should continue to be treated as a Federal budget receipt. But other receipts and expenditures of the Federal Reserve Banks should continue to be excluded from the budget. [3]

This presentation has been followed by Presidents Johnson, Nixon, Ford, Carter, and Reagan.

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[3] Report of the President's Commission on Budget Concepts, pp. 28-29. The third budget concept referred to is the National Income and Product Accounts, which includes Federal Reserve and other governmental transactions in its records of aggregate economic activity.

The Quasi-Private Status of the Federal Reserve Banks

The Federal Reserve Banks have retained some private characteristics that were established when the System was devised in 1913. Commercial banks that wish to be members of the System are required to purchase the capital stock of their Reserve Banks and are granted the right to select a majority of each Bank's directors. The act also requires that if the Federal Reserve is dissolved the capital subscriptions of member banks must be refunded before the remaining assets are turned over to the U.S. Treasury. A not uncommon belief is that these characteristics are cause for exclusion of the Banks from the budget.

In general, private ownership and control of an organization have been sufficient grounds for excluding the organization's finances from the budget, although the Budget and Accounting Act of 1921 does not require this. The degree of private ownership and control of the Federal Reserve Banks is limited, however. Ownership of Federal Reserve Bank stock is an obligation incident to membership in the System, and does not represent a full interest in Bank assets. 4/ Member banks participate with the Board of Governors in the selection of Bank directors, but the degree of control exercised by these directors is restricted. For example, the Board of Governors must approve the directors' nominees for the chief executive postions of the Banks and the salaries of Bank officers. The Board of Governors also reviews and approves the Banks' budgets and directs the Banks' implementation of System policies. Moreover, the role of the Federal Reserve Banks is to carry out governmental functions with governmental powers. It does not seem reasonable to consider the Federal Reserve Banks as nongovernmental, given their monetary and regulatory policy activities.

This interpretation that the Federal Reserve Banks are essentially governmental in character has been supported by the Board of Governors

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4. The money creation powers of the Federal Reserve System make capital subscriptions and the Banks' surpluses (retained earnings) unnecessary as sources of financing. Some have proposed that the System's structure be modernized by abolishing these vestigial characteristics, and by subsequently requiring the Federal Reserve Banks to submit business-type budgets under the Government Corporation Control Act (31 U.S.C. 9101).

and the courts in a number of instances. 5/ The courts have held that the Federal Reserve Banks are "independent, privately owned and locally controlled corporations" for certain limited purposes, but only when the Congress has specifically defined the Banks to be private in character. 6/ The courts have not issued any rulings on the question of whether the Banks have been considered by the Congress to be governmental or private organizations for the purpose of presenting their financial operations in the unified budget.

The President's Commission on Budget Concepts reviewed a paper that suggested that the Banks' private characteristics were grounds for excluding the Banks from the budget, but the Commission did not accept this reasoning. 7/ On the contrary, for the Commission wrote (as quoted above), "The System is clearly a Federal Government Operation." Nor is the language that exempts the Board of Governors, and by extension the Federal Reserve Banks, from the appropriations process and government audit the cause for the System's exclusion from the budget. This language was included in the Banking Act of 1933:

> The Board shall determine and prescribe the manner in which its obligations shall be incurred and its disbursements and expenses allowed and paid, and may leave on deposit in the Federal Reserve banks the proceeds of assessments levied upon them to defray its estimated expenses and the salaries of its members and employees, whose employment, compensation, leave, and expenses shall be governed solely by the provisions of this chapter and rules and regulations of the Board not inconsistent therewith; and funds derived from such assessments shall not be construed to be Government funds or appropriated moneys. 8/

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5. See, for example, the Board of Governors' response to a question posed by Representative Patman, in Joint Committee on the Economic Report, Monetary Policy and the Management of the Public Debt (1952), vol. 1, pp. 261-62; Raichle v. Federal Reserve Bank of New York, 34 F.2d 910 (2d Cir. 1929); Raymond Natter, "Legal Status of the Federal Reserve System," Congressional Research Service (March 3, 1983).

6. Lewis v. United States, 680 F.2d (9th Cir. 1982).

7. Elmer B. Staats, "Coverage of the Budget—Government-Sponsored Enterprises," in Staff Papers and Other Material Reviewed by the President's Commission (October 1967), pp. 187-95.

8. 12 U.S.C. 244.

Similar language was enacted for the Office of the Comptroller of the Currency, which also regulated banks, and for the Federal Deposit Insurance Corporation, which insured banks. Before the adoption of the unified budget, these agencies' finances were excluded from the administrative budget by virtue of their trust fund status. The revenues and expenditures of the Comptroller and FDIC are now included in the unified budget.

FEDERAL RESERVE FINANCES AND CURRENT BUDGET CONCEPTS

The President's Commission on Budget Concepts stated that "the nature and economic significance of Federal Reserve Bank 'receipts' and 'expenditures' are different from those of most other government programs and activities," and concluded that they should be excluded from the unified budget. This section examines the nature of Federal Reserve Bank finances and considers whether they could appropriately be shown in the budget given current budget concepts. 9/

Administrative Expenses and Offsetting Collections

In citing the different "nature and economic significance" of the Federal Reserve's financial operations, the President's Commission on Budget Concepts was obviously referring to the unique nature of the Federal Reserve's monetary policy activities. But the Banks' administrative expenses and offsetting collections, on the other hand, are no different from the expenses and collections of other federal agencies that are shown in the budget documents. Construction of a building, for example, whether by the Federal Reserve, General Services Administration, or Department of Defense, draws upon the supply of construction goods, employs labor in the building trades, and reduces the cash balances of the government. The Federal Reserve's payment to the Bureau of Engraving and Printing for currency, and its receipts from the Treasury and other agencies for fiscal agent services, are similar to the many intragovernmental transfers of funds made between agencies. Priced services fees are comparable to similar offsetting collections made by federal business-type enterprises like the Tennessee Valley Authority or the Federal Housing Administration. All of these expenses and receipts are included in the Federal Reserve's calculation of its payments to the Treasury, but they are not shown in the budget documents.

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9. The budget presentation for the Federal Reserve is compared to that for other off-budget organizations and for other organizations with activities similar to those of the Federal Reserve in Appendix A.

Monetary Policy Finances: Open-Market Transactions

The Congress has given both the Federal Reserve and certain trust and revolving funds authority to purchase and sell Treasury securities. These transactions may be distinguished by their different purposes and financing sources. The main purpose of purchases by trust and revolving funds is cash management, for funds often find that they have more cash on hand (from dedicated revenues, receipts from borrowing, and offsetting collections) than is necessary for immediate disbursement. In the case of some government funds, U.S. securities are accumulated to earn interest and lessen the need for subsequent appropriations to these funds.

The funds invest their temporary excesses of cash in government securities and receive interest payments, and the Treasury uses these temporary deposits to meet the cash needs of other programs. The securities assets of the funds are shown in Program and Financing Statements as unobligated balances, and are readily convertible to cash for payment of program obligations. Conversions of government securities to cash reduce the cash balances of the Treasury.

In constrast, Federal Reserve security purchases and sales are not carried out for cash management purposes, but to expand, stabilize, or contract the money supply. The Federal Reserve's financing practices also differ from those of government trust and revolving funds. The Federal Reserve finances its purchases by "writing a check on itself" through the creation of bank reserves. The authority to create bank reserves gives the Federal Reserve an unlimited capacity to purchase securities. A Federal Reserve purchase of Treasury securities does not increase the cash balances of the Treasury, for the Federal Reserve exchanges cash for securities with the private sector in the open market. When the Federal Reserve sells or exchanges maturing securities, this cash it obtains in exchange is not available to finance other government expenses, since the goal of security sales is to reduce bank reserves.

It is conceivable that a Program and Financing Statement for the Federal Reserve could include its securities transactions. The statement would show the net amount of bank reserves and currency created during the fiscal year as financing for the program obligations of the net security purchases during the fiscal year. On the other hand, the peculiar nature of Federal Reserve financing might preclude showing security transactions in this way. Federal Reserve transactions do not draw upon "budgetary resources" as conventionally defined--receipts from taxes, borrowing, or offsetting collections. 10/

It can be argued that monetary policy transactions should be shown in a Program and Financing Statement because the Federal Reserve's current net income is already included in the budget as a receipt. This income, which is transferred to the Treasury, is primarily derived from interest on government securities. Because the budget shows these interest earnings, it is argued, the budget should also show the financial transactions that lead to changes in the level of these payments. On the other hand, also excluded from the budget is information on the projected debt transactions of the Treasury, even though the budget includes projections of outlays for payment of interest on the debt. This limited presentation maintains the Treasury's flexibility to conduct debt financing operations.

Monetary Policy Finances: The Discount Window

Discount loans are financed by the creation of bank reserves, as are securities purchases. Yet the functions of discount loans differ from the functions of securities purchases in several respects. Over time, discount loans are a relatively unimportant factor in the growth of total reserves when compared to securities purchases. The main uses of the discount window are instead to serve the short-term credit requests of banks, to signal the direction of monetary policy through changes in the discount rate, to function as a tool of Federal Reserve regulatory power, and to supply large amounts of credit during a banking crisis. The first function, which

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10. Of all other federal programs, only the Treasury Department also makes transactions the primary purpose of which is the conduct of monetary policy. The Exchange Stabilization Fund's holdings of foreign currency are considered to be cash assets; changes in these holdings are outlays only to the extent there is a realized loss on currency exchanges, and are offsetting collections only to the extent there is a realized profit. Deposits with the International Monetary Fund are also considered to be similar to cash assets, and movement of money between the International Monetary Fund and the Treasury is excluded from budget totals.

often involves provision of a subsidy, is similar to the provision of below-market-rate loans by other government loan programs. 11/

When the Federal Reserve makes short-term loans--known as adjustment credits--it loans funds to banks at the discount rate. The discount rate is usually lower than the market rate charged for the alternative source of overnight funds for banks, the federal funds rate. If the difference between the discount rate and the federal funds rate is taken to represent the subsidy conferred on the borrowing banks, the subsidy for short-term (adjustment and seasonal) credit averages approximately $10 million to $30 million annually. In periods of peak interest rates and borrowing, the subsidy for short-term credit may amount to $100 million on an annual basis (the subsidy for extended credit was not estimated), and in other periods it may be negligible. 12/

The discount rate is also usually below the earnings rate on the Federal Reserve's portfolio of securities. If the money supply is to be unchanged, an increase in outstanding discount loans must be offset by a decrease in securities held by the Federal Reserve. The Federal Reserve consequently suffers the opportunity cost of an earnings loss when the earnings rate on its portfolio exceeds the discount rate. 13/ The earnings loss on short-term loans was approximately $20 million to $25 million in fiscal year 1984.

If the Federal Reserve's discount loans were included in the budget, neither the value of a subsidy to banks nor the opportunity cost of an earnings loss to the Federal Reserve would be shown. The budget instead would show the net cash flow of the discount loan program--the net of

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11. Depository institutions argue that the subsidy conferred by low-cost discount window funds is more than offset by the "reserve tax." The "reserve tax" is the earnings loss suffered by depository institutions on the non-interest-bearing funds on deposit with the Federal Reserve Banks that exceed the depository institutions' preferred level of reserves.

12. It should be noted that funds loaned at the discount rate are fully secured by collateral and that overnight federal funds are not. The risk of default on federal funds is extremely small, however.

13. The Federal Reserve minimizes its earnings loss on extended credit loans by charging discount rates that are roughly equivalent to the earnings rate on its portfolio.

current loan originations and repayments--which is the measure reported for other government loan programs. Almost all discount loans are repaid within the federal budget year, and such repaid loans are not shown--for any agency--as loan activity in the budget documents. Moreover, no cash outlays are made when a discount loan is originated, a result of using reserve creation as the source of financing. Using conventional cost concepts, as is the case with security transactions, the budget would not show any discount loan activity. (See the box on the following page on budget treatment of the discount loan to Continental Illinois.)

On the other hand, the Federal Reserve recognizes and reports a similar type of transaction that is financed through reserve creation--the advance of Federal Reserve float. Federal Reserve float results when banks are paid for deposited checks before the Federal Reserve collects on these checks. Additional reserves are created when float increases. As is the case with discount loans, an increase in Federal Reserve float must be offset by a decrease in securities held by the Federal Reserve if the money supply is to be unchanged. The Federal Reserve does not suffer an earnings loss, however, for under the Monetary Control Act of 1980 the Federal Reserve must charge interest on float at the federal funds rate. This policy, which eliminates the subsidy associated with float before 1980, is consistent with the policy contained in a recently released OMB Circular on credit programs. Circular A-70 of August 24, 1984, requires agencies to report the subsidy costs of federal loan programs. Given that the Federal Reserve already reports the levels of Federal Reserve float and charges for its subsidy value, it is plausible that the subsidy value of the discount window could also be reported by the Federal Reserve. In addition, a Status of Direct Loans schedule could show past and projected discount loan activity.

Monetary Policy Finances: Income from Securities

The deposit of Federal Reserve current income is presently included in the budget, where it is classified as a receipt. Government financial documents must show that the payment by the Federal Reserve to the Treasury reduces the need to borrow from the public in order to fund spending. Not all of the cash received by the Treasury is counted as budget receipts, however. Excluded from the budget are Treasury receipts from borrowing, profits from gold sales, and coin seigniorage, which are classified as a "means of financing" the deficit.

Most Federal Reserve current income results from currency and reserve seigniorage, made possible by the difference between the cost of producing currency and reserves and their value in exchange. The Federal Reserve's profits from money creation have been invested in securities and

Budget Treatment of the Continental Illinois Discount Loan

A Federal Reserve discount loan of $3.5 billion was recently assumed by the Federal Deposit Insurance Corporation (FDIC) as part of its assistance plan to Continental Bank of Illinois. In return for assuming Continental Illinois's debt of cash to the Federal Reserve, the FDIC acquired loans previously owned by Continental Illinois. Over the next five years, the FDIC will pay the interest and principal payments due on these loans to the Federal Reserve, and will finance any shortfalls from its collections on the loans by drawing down its fund. This financing procedure is not the normal method of providing assistance. Normally, the FDIC sells some of its securities to obtain the cash it provides to an assisted bank. In the Continental Illinois case, the Federal Reserve's discount window served as the source of financing.

The use of the discount window as a source of financing affected the budget treatment of the assistance to Continental Illinois. Normally, loans and equity assistance from the FDIC's fund are scored as contributing to outlays, and repayments of assistance are scored as offsetting collections. An FDIC sale of securities is reflected in a decrease in the fund's unobligated balances (its equity). In contrast, the Office of Management and Budget has chosen to show the assistance to Continental Illinois as outlays only if and when the FDIC's fund suffers losses.

This decision was based on the fact that the FDIC did not disburse cash to Continental Illinois nor draw down any of its equity. The cash assistance received by Continental Illinois was provided directly by the Federal Reserve. The FDIC simply acquired problem loans from Continental Illinois (which increased the FDIC's assets) in return for promising to pay off Continental Illinois's debt to the Federal Reserve (which increased the FDIC's accrued liabilities). The FDIC's exposure is similar to that from other assistance plans--the possibility that its new assets will not cover its new liabilities over the long run. Its current equity position, unlike in other assistance plans, was not affected.

The Continental Illinois loan is not recorded in the FDIC's budget because the FDIC did not provide any "budgetary resources," even though the FDIC did assume the risk of loss in the transaction. The loan is not recorded in the budget under the Federal Reserve's account because the discount operations of the Federal Reserve are excluded from the budget. The Federal Reserve is carrying the loan in its own books as an increase of $3.5 billion in its "Other Assets." The outcome of these decisions is that a government loan of $3.5 billion for a five-year term was not recorded for the 1984 budget.

foreign currencies and return a flow of income. 14/ Classifying Federal Reserve currency seigniorage in the same manner as coin seigniorage would be consistent with the economic nature of Federal Reserve current income. 15/ It would have the effect of reducing budget receipts and increasing the budget deficit, but the cash position of the Treasury would be the same. This effect is shown in the second column of Table 11.

Alternatively, since most Federal Reserve current income is from payments by the Treasury on its debt, Federal Reserve income could be seen simply as an intragovernmental transfer of funds. The Federal Reserve returns this income net of expenses to the Treasury on a weekly basis, and such intrayear transactions are not shown in the budget as program activities. Payments by the Treasury to the Federal Reserve could thus be netted from gross interest payments by the Treasury, much like the current treatment for other government funds (such as Social Security) that own Treasury securities. By classifying Federal Reserve interest income and Treasury receipts of Federal Reserve earnings as intragovernmental transfers, total budget outlays and receipts would be reduced by like amounts (assuming the Federal Reserve Bank's operating expenses were reported separately as outlays), as shown in the third column of Table 11. This net budgetary effect is currently reported in the budget as an addendum in the presentation of outlays in the net interest function. 16/ Table 12 shows the magnitude of Federal Reserve earnings transfers and of interest outlays net of these transfers from fiscal year 1970 to fiscal year 1983.

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14. See articles by Benjamin Klein, Harry G. Johnson, and Thomas F. Wilson in Kenneth F. Boulding and Thomas Frederick Wilson, Redistribution Through the Financial System, Praeger (1978), pp. 3-56.

15. The Report of the President's Commission on Budget Concepts stated, "The Commission recommends treating seigniorage as a means of financing rather than as budget receipts. Seigniorage does not involve a transaction with the public, and grows out of the exercise of the Federal Government's sovereign powers to create money, essentially equivalent in character to the issuance of bank notes (which happens to be a function of the central bank, rather than the Treasury in the United States, but which could easily be done by the Treasury)." (pp. 57-58).

16. The addendum shows the "net budgetary effects of interest transactions with the public" by deducting from gross interest outlays the interest paid to trust funds, interest on loans to the FFB, and the Federal Reserve's deposit of earnings, and by making several other

(Continued)

Summary: Budget Concepts

It is clear that Federal Reserve Bank administrative expenses and collections could be appropriately included in the budget given current budget concepts. Whether this holds for monetary policy finances, however, is less clear. Aspects of these finances--the purchase and sale of securities, the subsidy element in the discount loan program, and the transfer of funds to the Treasury--are similar to other government agency activities that are included in the budget. The Federal Reserve's unique ability to create money, on the other hand, is an ever present dissimilarity, one that has been used to justify excluding monetary policy finances from the budget. Yet, budget concepts are not immutable. It is conceivable that current budget concepts could be carefully extended to cover all of the Federal Reserve's monetary policy finances.

PREDICTABILITY AS A FACTOR

The President's Commission on Budget Concepts also cited as a reason for excluding the Federal Reserve Banks from the budget its belief that Federal Reserve Bank financial operations could not be projected with acceptable accuracy.

Treasury and OMB projections of Federal Reserve earnings are now provided in the budget documents. They are sensitive to variations in current income. The level of current income is dependent on conditions that may change unexpectedly and widely from the time of the budget projection to the end of the fiscal year. Forecasts of Federal Reserve current income combine economic assumptions for interest rates with projections of the size and maturity distribution of the Federal Reserve's portfolio. Projections of the Federal Reserve's portfolio are made from economic assumptions that include the level of nonborrowed reserves and currency, the level of real GNP, and the term structure of interest rates. In the past few years, forecasts of interest rates have been less accurate than have forecasts of other major economic variables. As a result, the fiscal year 1983 Treasury model estimating error for Federal Reserve earnings was $1.1 billion--that

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16. (Continued)
adjustments. The Treasury currently classifies Federal Reserve-owned Treasury debt as "debt held by public." To be consistent with the presentation of Federal Reserve earnings as either seigniorage or intragovernmental transfers, the classification of Federal Reserve-owned Treasury debt would have to be changed to "debt held by government." See also Congressional Budget Office, Federal Debt and Interest Costs (September 1984).

TABLE 11. THE UNIFIED BUDGET OUTCOMES OF FEDERAL RESERVE INCOME RECLASSIFICATION AND EXPENSE PRESENTATION
(In billions of dollars, hypothetical figures)

		Expenses Presented as Outlays	
	Current Presentation	Income as Seigniorage	Income as Intragovernmental Transfer
Outlays			
Net interest	90.0	90.0	74.5
Federal Reserve	0	0.5	0.5
All other	700.0	700.0	700.0
Total	790.0	790.5	775.0
Receipts			
From Federal Reserve	15.0a/	0	0
All other	585.0	585.0	585.0
Total	600.0	585.0	585.0
Deficit	190.0	205.5	190.0
Means of Financing b/	-0.5	-15.5	-0.5

SOURCE: Congressional Budget Office.

a. Federal Reserve gross receipts are assumed to be $15.5 billion and expenses are assumed to be $0.5 billion (net of collections). When receipts and outlays are netted, Federal Reserve earnings transferred to the Treasury are $15.0 billion.

b. Recorded as "transactions not applied to current year's surplus or deficit" in Treasury financial statements.

TABLE 12. FEDERAL RESERVE EARNINGS TRANSFERS AND NET BUDGETARY INTEREST (By federal fiscal year, in millions of dollars)

Year	Deposit of Earnings by the Federal Reserve System	Net Interest Outlays	Net Effect of Interest on Budget Deficit
1970	3,266	14,379	11,113
1971	3,533	14,840	11,307
1972	3,252	15,478	12,226
1973	3,495	17,349	13,854
1974	4,845	21,449	16,604
1975	5,777	23,245	17,468
1976	5,451	26,711	21,260
TQ	1,500	6,946	5,446
1977	5,908	29,878	23,970
1978	6,641	35,441	28,800
1979	8,327	42,615	34,288
1980	11,767	52,511	40,744
1981	12,834	68,734	55,900
1982	15,186	84,995	69,809
1983	14,492	89,774	75,282

SOURCE: Office of Management and Budget, "Federal Government Finances."

is, actual receipts were $14.5 billion and the estimate was $13.4 billion. The CBO estimating error was $-0.5 billion. Most of the error resulted from different economic conditions than expected, and the rest was caused by technical factors. The estimating error was relatively small in comparison to the estimating errors in other categories, in dollar terms, but relatively large in percentage terms.

Expenses and priced services fees are affected by changing economic conditions, but are relatively stable and may be forecast very accurately. From 1979 to 1983, actual expenses in service lines from 1979 to 1983 differed from Board-approved budgets by an average (the mean of absolute differences) of 6.1 percent. (These estimates were made just prior to the budget years.) Federal Reserve System projections of capital outlays consistently overestimated actual spending by an average of 28.7 percent in

1979-1983, reflecting the difficulty of projecting the timing of capital outlays and the low priority placed by the System on annual outlay estimates for capital purchases.

Were the budget documents to include projections of discount loans, the problem of predictability might be more serious. While the average level of Federal Reserve discount loans is relatively stable over time, its loan activity often varies by billions of dollars from day to day. Therefore, the level of loans on September 30th could be quite different from the average level for the period at the end of the fiscal year, "distorting" the figures shown in the budget. On the other hand, end-of-year financial transactions by some on-budget loans and insurance funds--such as the Farmers Home Administration and the FDIC--are also quite variable.

The potential error in predictions of net open-market transactions at year-end is also large. The Federal Reserve often trades several billion dollars of securities a day in response to technical market factors. This trading activity is unpredictable beyond a short-term period. The most reliable annual projections are based on growth trends and seasonal cycles, the method used in budget projections for other programs with highly variable rates of activity. If future activities are thought to be too unpredictable for projection, budget schedules could show only the actual discount loan and open-market transactions from previous years.

THE FEDERAL RESERVE'S INDEPENDENCE

The Commission's most important argument was that the independence of the Federal Reserve would be jeopardized by the inclusion of its finances in the budget. In particular, it felt that any requirement that the Federal Reserve Banks project their finances would amount to an announcement of future monetary policy. Projections by the Federal Reserve of its earnings could give an indication of its goals and expectations for money supply growth and interest rates. At present, this information is not revealed by the estimates in the budget documents, which are prepared by Treasury and OMB without assistance from the Federal Reserve. The CBO makes similar independent estimates for the budget baselines used in the Congressional budget process.

Ten years after release of the Commission's Report, the Congress enacted the Federal Reserve Reform Act of 1977 (P.L. 95-188). This law required the Federal Reserve to make public annual targets for growth in the money supply. Under this law and the "Humphrey-Hawkins" Act of 1978, the Federal Reserve provides the Congress with estimates for ranges of the money supply, interest rates, and other economic variables. It does not provide point estimates, with the assent of the Congress. Range estimates have been preferred to point estimates because of uncertainty about the course of the nation's economy and the variable relationship between monetary aggregates and economic activity.

As stated above, projections of Federal Reserve earnings are made from point estimates of interest rates and of the size and maturity distribution of the Federal Reserve's portfolio. Revelation of the Federal Reserve's point estimates of these factors would convey significantly more information about its plans than is currently contained in its wide range estimates of money growth and interest rates. For example, the Federal Reserve can affect money growth only to a degree, and the relationship between money growth and the Federal Reserve's policy instruments is complex. The Federal Reserve's portfolio, on the other hand, is its major policy instrument. If it was required to publish a specific projection of its portfolio size, this could serve as a benchmark for evaluation of its monetary policy performance. Whether or not the System's monetary policy performance should be made easier to evaluate is a subject beyond the scope of this paper.

A Federal Reserve projection of earnings might come to be seen as an operating target, creating pressure on the Federal Reserve to transfer the projected amount to the Treasury. Nearly all observers believe, however, that open-market transactions should be carried out only for monetary purposes, without concern for their effects on the fiscal condition of the government. To do otherwise--maintaining a portfolio large enough to return the projected earnings--could result in supplying an inflationary level of bank reserves to the economy.

Finally, the Federal Reserve's freedom to determine its operating expenditures could conceivably be threatened by including these expenditures in the budget documents. Making Federal Reserve Bank operating expenditures visible might lead proponents of reducing government spending to press for reductions in Federal Reserve operating expenditures in authorizing and/or appropriations acts. It should be observed, however, that almost all other independent agencies are included in the budget documents despite a similar threat to their spending flexibility.

THE MECHANICS OF BUDGET PRESENTATION

The actual form that budget presentation of Federal Reserve finances might take would depend on choices made by the Office of Management and Budget and the Congress. Most technical decisions on budget presentation are made by OMB, often after consultation with the Congress. These decisions are strongly influenced by interpretations of the statutes that govern agency finances.

Six major choices of budget presentation form exist for the Federal Reserve. They are:

- Whether to have a unified set of accounts for the System as a whole or separate accounts for the Board of Governors and the Federal Reserve Banks.
- Whether to have separate funds for the different programs of the System or a single fund. The number of funds and their types (federal or trust, for example) would be affected by the degree of Congressional and Presidential control over Federal Reserve expenses. Separate funds of different types could be established for monetary policy, supervision and regulation, market-oriented financial services, and government fiscal and financial services, for example. This choice would affect the allocation of outlays to budget subfunctions (likely candidates are in functions 370--Commerce and Housing Credit, and 800--General Government).
- Whether or not to include monetary policy finances as program obligations and financing sources.
- Whether or not to include Federal Reserve projections of monetary policy finances.
- Whether or not to report Federal Reserve discount loans as a loan operation in a Status of Direct Loans schedule.
- Whether to classify Federal Reserve income as budget receipts, as a means of financing the deficit, or as intragovernmental transfers in the net interest function.

Budget presentation of Federal Reserve finances would require it to provide budget submissions that are consistent with federal budget documents. At a minimum, this would mean changing from the calendar-year fiscal year to the federal fiscal year, expensing capital purchases, and recording obligations of Federal Reserve Banks. In addition, the System would need to estimate its operating expenditures beyond a single budget year. Current Federal Reserve Bank accounting, which converts its expenses to a private-sector basis, would have to be maintained for Monetary Control Act pricing purposes. Changes in budget preparation activities of this magnitude have been carried out by other government agencies in the past.

CHAPTER V. THE FEDERAL RESERVE SYSTEM AND THE APPROPRIATIONS PROCESS

The Congress has developed three basic processes by which it reviews government agency spending. The Federal Reserve System is subject to two of these processes--authorizing legislation and oversight--but not to the third, the appropriations process.

The freedom of the Federal Reserve to make important decisions without prior appropriations approval from the Congress has implied to some that the Federal Reserve spends more than is necessary. Some also contend that the Federal Reserve's freedom violates the principle that government should be accountable for the money it spends. Accordingly, repeal of the Federal Reserve System's exemption from the appropriations process has been proposed. 1/ Against this it can be argued that the Federal Reserve System's appropriations independence is justified by the unique nature of the functions it performs. In addition, existing oversight and authorization controls on the Federal Reserve System's spending and policy decisions are thought to foster accountability to the public.

Outline of the Chapter

This chapter considers the important question of whether the Federal Reserve's exemption from the appropriations process should be repealed. The first section describes the three basic spending control processes. It provides examples of how the Congress could use the appropriations process to direct the Federal Reserve, and reviews the recent authorizing and oversight activities of the Congress relating to the Federal Reserve. This section concludes by describing some of the criteria that the Congress has considered to be important when deciding whether to apply the appropriations process to particular agencies. Three of the most important criteria are the potential effects of the process on spending efficiency, on budget

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1. In the 98th Congress, bills that would subject the Federal Reserve System to the appropriations process included: H.R. 3530, Conyers (D-MI); H.R. 4569, Vento (D-MN); and S. 10, Cranston (D-CA). Bills in the 97th Congress were: H.R. 5066, Conyers (D-MI); S. 1691, Hawkins (R-FL); and H.R. 6639, Patterson (D-CA).

savings, and on policy direction. These considerations form the basis for the remaining three sections of the chapter.

The second section reviews three methods of evaluating the spending record of the Federal Reserve: comparing the growth rates of Federal Reserve and other agency spending, comparing Federal Reserve and other agency objects of expense costs, and judging the Federal Reserve's success in complying with the market test constraint of the Monetary Control Act. A detailed comparison of personnel compensation policies is included to emphasize the complexity of such evaluations.

The third section of the chapter provides illustrations of budget savings approaches for the Federal Reserve. These include spending ceilings and also spending reductions for specific purposes, approaches that are commonly used in the appropriations process. Other savings approaches are more commonly used in authorizing legislation, including cost recovery, privatization, and administrative restructuring. The chapter closes with an analysis of the potential use of the appropriations process to direct Federal Reserve regulatory and monetary policy.

CONGRESSIONAL SPENDING CONTROL PROCESSES

The Congress uses three basic processes to authorize and control spending by individual agencies--the appropriations, authorization, and oversight processes. 2/ This section describes the characteristics of these processes. It also provides examples of how the Congress could potentially direct the Federal Reserve through the appropriations process, and describes how the Congress has reviewed and directed the Federal Reserve through recent authorizing and oversight actions.

The Appropriations Process

In the appropriations process the Congress passes acts that provide authority for agencies to incur obligations and make payments out of the Treasury for specified purposes. Thirteen regular acts of this type are prepared and reported each year by the House and Senate Appropriations Com-

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2. Supplementing these basic processes is the budget process established by the Congressional Budget Act of 1974 (P.L. 93-344), through which the Congress sets aggregate spending goals to guide the authorization and appropriations processes.

mittees. Supplemental and continuing appropriations acts are also routinely considered by the Congress.

The appropriations process is the procedure used to control the administrative expenses of most federal agencies. Appropriations acts generally set limits on the yearly expenditures of agencies for certain broad categories, such as "salaries and expenses." Spending within these categories is often directed by statements in Appropriations Committee reports (or on the floors of the House and Senate) that describe the expected distribution of funds to activities. Activities may be specified to the level of individual projects. Agencies generally follow these directions, but occasionally request permission from the Committees to reprogram funds to other activities.

Appropriations acts may also contain provisions that restrict spending for certain purposes or objects of expense. These provisions (called "riders") may, for example, limit the number of personnel hired by an agency or prohibit spending to enforce a specific regulation. Riders that do not merely restrict spending, but also make policy, are called "legislative" riders. Legislative riders must generally receive waivers from the House and Senate rules to remain in an appropriations bill. If waivers are not received, points of order may be raised (and frequently are) to strike the legislative provisions from the bill. Finally, in recent years limits on direct loan obligations and loan guarantee commitments have been included in appropriations bills.

Making the Federal Reserve System subject to the appropriations process would allow the Congress to set the level of Federal Reserve System spending annually and to allocate funds to specific purposes. For example, the System could be prohibited from spending more than $695.6 million on salaries and expenses (the actual level of personnel and retirement spending in calendar year 1983), or it could be directed to spend a certain amount in the Kansas City district. The Congress could conceivably also set specific limits on discount loan activities and securities and foreign currency transactions. Use of the appropriations process could also force the Federal Reserve to provide the Congress with more detailed information about its spending plans, and would give the Congress a convenient, annual opportunity to direct Federal Reserve policy. For example, the System could be directed by a rider to take actions to ensure that growth of the money aggregate M1 fall within the range of 6 to 9 percent or that the prime rate not exceed 10 percent in an upcoming fiscal year. Or it could be ordered not to process applications for bank holding companies to operate new "nonbank banks" in the upcoming fiscal year, or to end its subsidization of automated clearinghouses. These specific examples are merely illustrations of the potential uses of the appropriations process. The merits and drawbacks of selected appropriations limitations are discussed below.

Authorizing Legislation

Authorizing legislation sets up or continues the legal operation of an agency or program, or sanctions a particular type of obligation or expenditure within a program. Legislative jurisdiction for the Federal Reserve System is currently held by the House Banking, Finance and Urban Affairs Committee and the Senate Banking, Housing and Urban Affairs Committee. Authorizations may expire periodically (in some cases annually) or may be permanent. They may instruct an agency in great detail how to carry out specific activities, or may charge an agency with the duty to achieve broad goals with a program of its own design. Most authorizations for Federal Reserve activities are permanent and unspecific. Open-market operations, for example, are to

> . . . be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country. 3/

Authorizing legislation may also structure the financial operation of an agency or program. Some authorizations set a ceiling on budget authority to be included in appropriations acts, whereas others authorize "such sums as may be necessary," leaving the spending maximum to the discretion of the appropriations process. Other authorizations grant agencies the right to spend funds without being subject to the annual appropriations process. This spending is known commonly as "direct spending" and takes several forms. Some agencies have the right to borrow, to contract, or to pay funds to legally-eligible beneficiaries ("entitlement" payments), before receipt of appropriated funds. Treasury funds are available automatically to selected agencies through a "permanent appropriation." Some agencies possess authority to make expenditures out of a revolving fund financed with collections from a business-type operation, tax revenues that have been earmarked for that fund, or appropriations made in prior years.

Numerous legislative authorizations have affected the Federal Reserve System's financial operations. Changes in banking laws directly affect Federal Reserve System spending by, for example, increasing the workload for review of bank holding company applications. The most important authorizing legislation spending limit is the requirement of the Monetary Control Act of 1980 that the Federal Reserve Banks recover the costs (adjusted to a private-sector cost basis) of their services to financial institutions. The Federal Reserve Act requires that cumulative expenditures by the Federal Reserve Banks on branch buildings cannot exceed a $140 million

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3. 12 U.S.C. 263(c)

ceiling (with cost valued at book and depreciated over a 50-year period). 4/ Certain governmentwide personnel policies also must be followed by the System. Contractors with the Federal Reserve Banks, for example, are required by the Service Contract Act to pay minimum wages and fringe benefits for service workers. The Federal Reserve Banks became subject to this act following a ruling of the U.S. District Court of the District of Columbia in 1979. The applicability of other personnel and procurement policies to the Federal Reserve System depends on the construction of the statute establishing the policy (some statutes have explicitly or implicitly exempted the Federal Reserve System) or on the decision of the System to conform with the policy voluntarily.

Oversight

Oversight is review by the Congress of actions of the executive branch, and particularly of the interpretation and implementation of policy by federal agencies. It can take many forms, including hearings, studies, GAO audits, formal investigations, and letters to the agency with comments or questions from Members. Oversight of the Federal Reserve is generally carried out by the Joint Economic Committee, the Banking Committees, and the Government Operations Committee in the House and the Governmental Affairs Committee in the Senate. Oversight activities are generally not required, but are carried out at the initiative of a committee.

Congressional oversight of the Federal Reserve in recent years has been concentrated in four areas: economic policy, banking regulation, implementation of the Monetary Control Act, and the Federal Reserve System's budgets. The Federal Reserve is required to report semiannually on its targets for growth in the money supply and to comment on the consistency of its monetary targets with the economic objectives (for output, employment, and prices) of the President. The Chairman of the Board of Governors, other Governors, and Presidents of Reserve Banks regularly appear before the Banking Committees, the Joint Economic Committee, the Budget Committees, and other committees to discuss economic conditions, monetary policy, and fiscal policy. Domestic and international economic policy was the focus of over half of the 33 appearances made by Governors in

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4. H.R. 4009, reported on April 24, 1984, by the House Banking Committee, would have increased this ceiling to $200 million. See Federal Reserve System Modernization Act, House Report 98-694.

1983. 5/ Oversight of Federal Reserve monetary policy is limited by the traditional practice of permitting the Federal Reserve to decline to discuss in detail recent policy decisions or the reasons for them. Members objecting to the vague character of Federal Reserve reporting have proposed that it eliminate the month-long delay in revealing FOMC decisions and end the use of wide target ranges. 6/ The Federal Reserve has resisted these requests, claiming that these changes would encourage speculation in the securities markets. It also argues that the case for full disclosure presumes less uncertainty about the course of the economy than is actually present.

In recent years, the Banking Committees have annually reviewed the regulatory policies of the Federal Reserve System, responding to the rapid deregulation in the banking sector. 7/ The Congress has also reviewed the Federal Reserve's implementation of the Monetary Control Act in oversight hearings held by the Banking Committees and the House Government Operations Committee's Subcommittee on Commerce, Consumer and Monetary Affairs. These committees have also sent written comments to the Federal Reserve's docket on pricing decisions and have requested two GAO studies. 8/ Reviews of Federal Reserve System budgets were performed

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5. See Senate Banking, Housing and Urban Affairs Committee, First Monetary Policy Report for 1984 (March 28, 1984), and House Banking, Finance and Urban Affairs Committee, Monetary Policy Report (December 6, 1983).

6. See Legislation for Alternative Targets for Monetary Policy, Hearings before the Subcommittee on Domestic Policy, House Committee on Banking, Finance and Urban Affairs (April 26, May 11, and August 3, 1983) and remarks of Representative Jack Kemp (R-NY), "Federal Reserve Reform Legislation Open and Predictable Monetary Policy," Congressional Record, H2930-2 (April 12, 1984).

7. See Financial Services Industry Oversight, Hearings before the Senate Banking, Housing and Urban Affairs Committee (April 6-June 29, 1983).

8. General Accounting Office, "An Examination of Concerns Expressed About the Federal Reserve's Pricing of Check Clearing Activities" (January 14, 1985); General Accounting Office, "The Federal Reserve Should Move Faster to Eliminate Subsidy of Check Clearing Operations" (May 7, 1982); The Role of the Federal Reserve in Check

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from 1977 to 1980 by the Senate Banking Committee. The GAO has also prepared several studies on selected Federal Reserve expenditures. 9/

Arguments For and Against Appropriations

The Congress has made the administrative expenses of almost all federal agencies subject to control through its annual appropriations process. The appropriations process has proved attractive primarily because it allows the Congress to make very specific decisions about agency spending. Appropriations reviews are based on detailed justifications of spending plans by the agencies. Regular review of spending justifications permits the Congress to become knowledgeable about programs and encourages agencies to describe accurately their plans and carry them out in good faith.

Unlike the oversight process, in which committees are limited to review of expenditures after the fact or to suggestions for future spending directions, the appropriations process requires the Congress to act before an agency can obligate funds. If the necessary regular, supplemental, or continuing appropriations are not enacted, the agency must shut down nonessential operations or be in violation of the Anti-Deficiency Act. Unlike most authorizations, appropriations bills are considered annually, according

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8. (Continued)
Clearing and the Nation's Payment System, Joint Hearings before the Subcommittee on Domestic Monetary Policy, House Committee on Banking, Finance and Urban Affairs, and the Subcommittee on Commerce, Consumer and Monetary Affairs (June 15-16, 1983); Report of the House Committee on Government Operations, Federal Reserve Competition with the Private Sector in Check Clearing and Other Services (April 11, 1984); Federal Reserve Pricing Policy on Check Clearing Services, Hearings before the Senate Banking Committee (April 11, 1984); The Role and Activities of the Federal Reserve System in the Nation's Check Clearing and Payments System, Report of the Subcommittee on Domestic Monetary Policy, House Committee on Banking, Finance and Urban Affairs (November 1984).

9. 1980 Budgets of the Federal Reserve Bank Regulatory Agencies, Hearings before the Senate Committee on Banking, Housing and Urban Affairs (January 25, 1980), General Accounting Office, "Response to Questions Bearing on the Feasibility of Closing the Federal Reserve Banks" (May 21, 1981), and "Information on Selected Aspects of Federal Reserve System Expenditures" (February 12, 1982).

the opportunity for yearly adjustments in spending levels or policy direction through riders.

Finally, the appropriations process offers the Congress an opportunity to compare the relative merits of the different spending proposals of many agencies and to choose among them. This opportunity is constrained by the fact that less than half of the budget authority (43 percent in 1985) is subject to control by the annual appropriations process, because so-called "direct spending" programs have been excluded from appropriations control. Some direct spending programs could easily be converted to appropriated programs should the Congress wish to increase the comprehensiveness of the appropriations process.

Despite its advantages, the appropriations process is neither equally nor universally applied by the Congress to programs that are subject to it. A major limitation is the time required to review a specific agency or program. The Congress attempts to cope with this problem by concentrating its attention where it can have the greatest impact. Certain agencies with records of good management and budgeting often receive less scrutiny in the appropriations process than those with ineffective spending records.

Another limit on the efficacy of the appropriations process is the effect of prior decisions made during the authorizations process. Although the appropriations process is formally the point of discretion for the legal obligation of funds for many programs, authorizing legislation may greatly affect the amount of spending by setting the goals of programs and by structuring agency operations. Consequently, spending reductions in certain objects of expense (travel, for example) made in the appropriations process may be less effective as controls on spending than are changes in agency goals and operations made in authorizing legislation. Furthermore, spending limits set through the appropriations process may be inappropriate for programs designed to react on a day-to-day basis to changing markets. Only half of the government's business-type enterprises are subject to the appropriations process, with the Congress relying instead on oversight and authorizing legislation to review and control their finances. 10/

Finally, it is clear that certain agencies have been exempted from the appropriations process because the Congress has decided to insulate them from direct Congressional influence. The Comptroller of the Currency and

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10. Ronald C. Moe, "Administering Public Functions at the Margin of Government: The Case of Federal Corporations," Congressional Research Service (December 1983).

the Federal Deposit Insurance Corporation, two agencies with activities similar to the Federal Reserve's regulatory activities, are exempt. 11/

ALTERNATIVE METHODS OF EVALUATING THE SPENDING RECORD OF THE FEDERAL RESERVE

The ability of the Federal Reserve to draw on its open-market income to fund expenses without annual Congressional approval has implied to some that the Federal Reserve spends more than is necessary. By "more than necessary," critics have meant that they believe that the Federal Reserve has purchased higher quantities of goods and services than was needed, at higher prices than paid by other government agencies.

CBO cannot pass judgment on this charge. To do so would require inherently political, value-laden choices of the preferred quantity of activities to be carried out by the Federal Reserve, and the preferred tradeoff between the quality and price of Federal Reserve-purchased goods and services. It would also require an exhaustive audit review of the Federal Reserve.

Instead, this section illustrates three basic methods of evaluating the Federal Reserve's spending record: by comparing Federal Reserve and other agency spending growth rates; by comparing Federal Reserve and other agencies' objects of expense costs, with an emphasis on personnel compensation; and by reviewing the Federal Reserve's record in complying with the market test constraint of the Monetary Control Act. The latter method has been used in reviews of Federal Reserve spending by the House Government Operations and Banking Committees, the General Accounting Office, and the competitors of the Federal Reserve in the financial services markets.

Program Spending Growth

Comparisons of Federal Reserve spending growth with that of similar government agencies run up against two obstacles. One is the lack of com-

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11. For fuller descriptions of the factors that the Congress has considered to be important to the choice for or against appropriations, see Allen Schick, Legislation, Appropriations, and Budgets: the Development of Spending Decision-Making in Congress, Congressional Research Service (May 1984); and Louis Fisher, "The Authorization-Appropriations Process in Congress: Formal Rules and Informal Practices," Catholic University Law Review, vol. 29 (Fall 1979), pp. 51-105.

parable accounting practices. The Federal Reserve Banks capitalize capital purchases while other agencies do not. The Federal Reserve Banks do not record obligations--the focus of federal agency accounting. In Table 13, Federal Reserve Bank expenses were adjusted to approximate regular federal budget accounting practice, which expenses rather than capitalizes capital purchases. The other accounting disparities may be moderated by comparing rates of growth of spending over time. (The standard period used for comparison is 1979-1983, in calendar years for the Federal Reserve and in fiscal years for other agencies.)

TABLE 13. TOTAL FEDERAL RESERVE SYSTEM EXPENSES, CALENDAR YEARS 1979-1983 (In millions of dollars)

	1979	1980	1981	1982	1983	Average Annual Rate of Growth (Percent)
Board of Governors a/	52.7	61.5	59.7	66.2	70.7	7.6
Federal Reserve Banks b/	727.1	851.7	974.2	1,064.5	1,067.0	10.1
Net of Collections and Reimbursements	658.3	776.9	748.2	602.0	494.2	-6.9

SOURCE: Board of Governors of the Federal Reserve System, Annual Reports (1979-1983).

a. Board of Governors expenses are obligations as reported in the Budget Appendix.

b. Federal Reserve Banks expenses are adjusted, excluding the cost of currency and earnings credits, and replacing buildings and equipment depreciation with actual capital outlays.

A further complication is the choice of federal government spending activities to which the Federal Reserve's can appropriately be compared. Two areas of Federal Reserve activity--services to the financial sector and to government agencies--lack clear parallels in federal agency activities. In the areas of economic policy and financial regulation, however, the operating expenses of the Federal Reserve are quite similar in character to those of other agencies. The obligations of these agencies are shown in Tables 14 and 15. Tables 16 and 17 show the composition of Federal Reserve Bank current expenses and Board of Governors program obligations. 12/

TABLE 14. SELECTED ECONOMIC STATISTICS AND POLICY EXPENSES, FISCAL YEARS 1979 AND 1983
(In millions of dollars)

	1979	1983	Average Annual Rate of Growth (Percent)
Bureau of Economic Analysis	14.6	19.1	7.0
Bureau of Labor Statistics	93.0	130.0	8.7
Council of Economic Advisers	2.0	2.2	2.4
Office of Management and Budget	27.5	35.0	6.2
Office of the Secretary of the Treasury	63.0	80.2	6.2

SOURCE: Executive Office of the President, The Budget of the United States Government (fiscal years 1979-1983).

NOTE: Figures are program costs for economic analysis in the Bureau of Economic Analysis and total obligations for other agencies. Fiscal year 1979 expense categories adjusted to fiscal year 1983 expense categories.

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12. Expenses unadjusted to federal accounting treatment of capital are shown for the Federal Reserve Banks because capital outlays are not distributed to service lines by the Planning and Control System reports. The largest difference between adjusted and unadjusted total expenses in the period was 9.9 percent of total unadjusted expenses.

TABLE 15. ADMINISTRATIVE EXPENSES OF FEDERAL AGENCIES WITH FINANCIAL REGULATION DUTIES, FISCAL YEARS 1979-1983 (In millions of dollars)

	1979	1983	Average Annual Rate of Growth (Percent)
Comptroller of the Currency	96.6	144.2	10.5
Federal Deposit Insurance Corporation	107.7	138.2	6.4
Federal Home Loan Bank Board Total	49.2	67.0	8.0
Examinations and supervision only	28.9	32.3	2.8
National Credit Union Administration Total	20.3	27.6	8.0
Examinations and supervision only	15.7	18.8	4.6
Securities and Exchange Commission	66.5	87.8	7.2
Federal Trade Commission	65.0	67.3	0.9

SOURCE: Executive Office of the President, The Budget of the United States Government (fiscal years 1979-1983).

NOTE: Total obligations are shown for all agencies, with the exception of the Federal Deposit Insurance Corporation (FDIC). The administrative and operating obligations of the FDIC are reported, excluding the costs of closed bank activities. Examination and supervision expenses only are also reported for the Federal Home Loan Bank Board and the National Credit Union Administration. Board of Governors expenses for the Divisions of Supervision and Regulation and Consumer and Community Affairs grew at a rate of 8.7 percent from 1979-1983.

TABLE 16. COMPOSITION OF FEDERAL RESERVE BANKS' CURRENT EXPENSES, 1979-1983
(In millions of dollars)

	1979	1980	1981	1982	1983	Average Annual Rate of Growth (Percent)
Monetary and Economic Policy	38.2	59.6	81.2	93.0	100.4	27.3
Services to U.S. Treasury and Government Agencies	83.5	92.5	93.4	115.1	120.3	9.6
Services to Financial Institutions and the Public	500.3	554.7	611.6	646.2	675.9	7.8
Supervision and Regulation	71.7	86.1	99.9	119.3	131.8	16.4
Total	693.7	792.9	886.1	973.6	1,028.5	10.4

SOURCE: Planning and Control System (PACS) expense reports. The costs of Federal Reserve Note issue, which are included in PACS reports from 1979 to 1982, are not shown. The costs of monitoring reserve accounts are included in the supervision and regulation service line.

TABLE 17. COMPOSITION OF BOARD OF GOVERNORS PROGRAM OBLIGATIONS, 1979-1983
(In millions of dollars)

	1979	1980	1981	1982	1983	Average Annual Rate of Growth (Percent)
Formulation of Monetary Policy	11.8	13.1	14.2	15.2	16.1	8.1
Supervision and Regulation of Financial Institutions a/	10.7	11.9	12.7	13.7	15.4	9.5
Financial Services for System, Government and Public	0.6	0.8	0.8	0.9	0.7	3.9
System Policy Direction and Support, and Capital Investments	29.5	35.8	31.9	36.4	38.5	6.9
Total b/	52.7	61.5	59.7	66.2	70.7	7.6

SOURCE: Executive Office of the President, The Budget of the United States Government (fiscal years 1979-1983).

a. These obligations include not only those for bank supervision and regulation, but also those of Reserve Bank supervision. Board of Governors expenses for the Divisions of Supervision and Regulation and Consumer and Community Affairs grew at a rate of 10.3 percent from 1979 to 1983.

b. Details do not add because of rounding.

These tables show that the rate of growth of Federal Reserve Bank spending for economic policy (Table 16) was far greater than that of the economic policy agencies in Table 14 (all of which are subject to the appropriations process). Spending by the Board of Governors (Table 17) grew at a rate lower than that of the Banks, somewhat higher than the rate for the Office of Management and Budget, the Council of Economic Advisers, and the Office of the Secretary of the Treasury, but similar to the rates for the Bureau of Economic Analysis and the Bureau of Labor Statistics. Federal Reserve Bank spending in the regulatory area also grew faster than spending by comparable regulatory agencies shown in Table 15 (only the FHLBB, SEC, and FTC are subject to the appropriations process). 13/

Simple comparisons of growth rates can be misleading, for differences between the growth rates of spending by these agencies may reflect different legislative requirements and program factors. Recent spending by the Federal Reserve has increased in part because of legislative requirements, particularly the Monetary Control Act's establishment of universal reserve requirements and service pricing. Other significant factors in spending growth of the System--such as the adoption of contemporaneous reserve accounting--appear to have been regarded in the Congress as being justified, although the Congress did not give specific prior approval for the costs of such actions. In the regulatory area, the Federal Reserve is responsible for regulating the rapidly growing number of bank holding companies. Its spending on bank examination has risen in response to the financial problems of many large banks. CBO did not attempt to compare the spending productivity of the Federal Reserve and the other agencies because of the substantial technical difficulties this task would present. 14/

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13. If the costs of monitoring reserve accounts are excluded from the supervision and regulation service line (the main purpose of reserves being to enhance the Federal Reserve's ability to control the money supply, not to ensure safety and soundness), Federal Reserve Bank spending grew by nearly 16 percent during the period.

14. For example, spending on supervision and regulation is partially a function of the different methods and frequencies of examination used by the agencies and of the relative risks presented by the groups of banks they supervise. Relatively arbitrary assumptions must be made about these factors to evaluate the benefits associated with the agencies' different spending levels. See Leonard Lapidus and others, State and Federal Regulation of Commercial Banks, (Federal Deposit Insurance Corporation, 1980); General Accounting Office, "Comparing Policies and Procedures of the Three Bank Regulatory Agencies" (March 29, 1979).

Objects of Expense: Personnel

A second approach to reviewing the spending record of the Federal Reserve is to compare spending on particular objects of expense. Critics have sometimes focused on examples of spending that would not be permitted for other government agencies—the classic example being Representative Wright Patman's censure of the Federal Reserve Bank of Dallas for its purchase of ping pong balls.

The Federal Reserve's spending on decorative art can be compared with that of other agencies. The General Services Administration's "Art-in-Architecture" program for the buildings used by most federal agencies allows a set-aside of 0.5 percent of a building's construction or major renovation cost to be used for commissioning and installing permanent works of art. Only $7 million was spent under this program from 1962 to 1983, amounting to 0.2 percent of total cost. The Board of Governors allows, for the purchase of fixed and portable art, one dollar per square foot of building area (excluding parking structures) up to a maximum of 500,000 gross square feet, and 50 cents per square foot above this size. The art purchase allowance for the recently constructed Miami branch building was $256,000, of which $140,000 was spent, including a sculpture with a book value of $87,000. This was 1.1 percent of the total construction cost (excluding the special safekeeping costs of the Federal Reserve) of $12.6 million. The Board of Governors also has an extensive art program.

More significant comparisons can be made of spending for personnel, buildings, equipment, and major administrative overhead. Aspects of the Federal Reserve System spending on these major objects—salaries that in some cases exceed the maximum pay for other federal workers, the imposing, monumental design of Federal Reserve Bank buildings, the System's rapid acquisition of currency counters, check reader/sorters, and computers, and the large number of employees in overhead activities--suggest that savings could be made if certain expenses were limited.

To focus on expenses that would be prohibited for other federal agencies could be misleading, however. For example, in 1984, 125 Bank officers were paid above the Senior Executive Service pay ceiling of $70,000, for a total of $2.1 million, with the New York Federal Reserve Bank president receiving the System's highest salary of $176,100. But these higher expenses are at least partially offset by personnel compensation policies that allow the System to spend less than a federal agency would in other instances. For the other major objects of expense, simple comparisons of agency and Federal Reserve costs could also be misleading. In the building area, where account must be taken of the need of the Federal Reserve to construct and secure expensive vaults, one would expect square footage costs to be higher than those for a regular federal office building. Higher outlays for equipment may be wholly or partially offset by reductions in costs from the use of new technology, particularly reductions in labor costs.

Quantitative analyses of objects of expense are beyond the scope of this study. In the remainder of this section, however, the System's personnel policies are compared to those of federal civilian agencies. Personnel costs account for approximately 60 percent of the System's annual budget. The Federal Reserve's personnel policies reflect its decentralized structure, its tradition of directly comparing itself to the private financial industry, and its exemption from standard federal government personnel policy controls.

Federal Reserve Banks. Generally, the Federal Reserve Banks' policy is to base personnel compensation practices on those followed by the private sector, which are often quite different from those followed by federal agencies. 15/ Salary determination for employees is made on the basis of annual surveys in each branch; salaries for officers are based on a biennial national survey. The use of local wage rates for professional and support employees allows the Federal Reserve to pay salaries that reflect local conditions; this is not an option for federal agencies, which generally must pay the same salary for equally graded workers in high- and low-cost areas. Annual cost-of-living adjustments to salaries are not mandatory—the Banks use performance-based evaluations to determine promotions and raises. The Board of Governors has the authority to approve the compensation of Bank officers and to review the compensation of Bank employees.

Bank employees participate in Social Security and the System's Retirement Plan. The Banks pay the full cost of the retirement plan. Benefit adjustments for retired Bank employees (projected to equal about 60 percent of the annual change in the Consumer Price Index) are more than half again as high as those of average private-sector pension plans, but less liberal than those of the federal Civil Service Retirement program. Bank employees are also eligible to participate in a System-provided savings plan. The Thrift Plan's options include a traditional savings option, an IRA option, and a 401(k) deferred compensation option. The Federal Reserve matches employee contributions at a rate of 40 percent up to 6 percent of an employee's

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15. For an overview of federal personnel policies, see Robert W. Hartman, Pay and Pensions for Federal Workers (Brookings, 1983) and Jane Pernice Lundy, The Federal Employees Health Benefits Program: Issues and Problems, Congressional Research Service (February 6, 1984); basic Federal Reserve System salaries and benefits practices are described in a GAO report, "Information on Selected Aspects of Federal Reserve System Expenditures" (February 12, 1984), pp. 6-11.

income, a rate that is low compared to those typically sponsored by financial institutions. The deferred compensation option is an especially attractive method of sheltering income for many employees because contributions are in pre-tax dollars and distributions after age 59 and 1/2 or in case of hardship are eligible for 10-year averaging. In 1983, 19,929 Federal Reserve Bank employees participated in the Thrift Plan, contributing an average of $1,957. System contributions totalled $8,422,394, an average of $423 per participating employee.

The Banks pay the full costs of life and disability insurance for employees. They also pay all or nearly all of health insurance premiums for employees and from 50 percent to 66.7 percent of employee family premiums. Employer-paid health insurance is common for private employees, while in the Federal Employees Health Benefits Plan the government's maximum contribution is 75 percent of the total premium. On the other hand, Bank employees have many fewer plans from which to select a provider compared to federal employees, and certain high-cost services (mental health and drug abuse services) are not covered to the degree they are in the Federal Employees Health Benefits program. The Banks also provide dental insurance, deeply subsidized cafeterias, exercise facilities, and wellness programs.

Board of Governors. Personnel compensation practices of the Board of Governors are patterned after those of civilian federal agencies, but they are not identical. The Chairman of the Board of Governors is paid $72,600, the salary for deputy secretaries of major federal departments and for Members of Congress; other Board Members are paid $71,100. Merit pay is discretionary, the Board being exempt from the Civil Service Reform Act of 1978. The pay schedules for employees corresponds to the General Schedule used for Executive Branch employees. The Board has its own retirement plan, which is separate from but nearly identical in benefits to the Civil Service Retirement plan; its military service credit is less liberal. Board of Governors employees may participate in the Thrift Plan, while no employees of on-budget federal agencies have this opportunity at present. The Board contracts for life insurance benefits with the Federal Employees Group Life Insurance program and with a separate plan cosponsored by the FDIC and the Comptroller of the Currency. The Board covers one-third of the cost of life insurance premiums (the same percentage paid by federal agencies), but costs to the Board of Governors and employees for contributions are lower than the costs for federal agencies, because of the expectation that the largely professional Board of Governors work force will be longer-lived than the federal work force. Most Board employees participate in a Board-negotiated Blue Cross-Blue Shield health plan. Dental insurance and deeply subsidized cafeterias are also made available to Board of Governors employees.

Effects. It is clear that exemption from standard personnel compensation policies allows the Federal Reserve to offer its employees certain benefits that exceed in value those received by other federal civilian employees. Direct costs associated with these benefits--whether from dental premiums, salary amounts above the pay ceiling, or Thrift Plan contributions--have no counterpart in the operating expense accounts of on-budget agencies. The exemption may also enable the Federal Reserve to attract and retain high-quality personnel.

The Federal Reserve also bears the costs of separate contract negotiations, record-keeping, and information distribution. For most on-budget agencies these costs are borne by the Office of Personnel Management. Yet the greater flexibility enjoyed by Federal Reserve personnel management may also lead to more cost-effective spending, as is the case with the Banks' Retirement Plan. Federal Reserve salary costs are below those that would be paid by civilian agencies in certain regions of the country. Had the Federal Reserve Banks not been exempt from reduction-in-force guidelines, the substantial personnel reductions made in 1974-1983 (a decrease of about 4,700 workers, or 17 percent of the 1974 work force) could have been impeded. 16/ The Federal Reserve Banks are also not subject to appropriations limitations on permanent positions (slot ceilings), which are widely believed to encourage wasteful end-of-year spending and upward grade creep. 17/

The Market Test: Priced Services

A third approach to evaluating the Federal Reserve's spending record is to review its recovery of the costs of payments services through explicit pricing. As described above, prior to the Monetary Control Act, Federal Reserve payments services were available only to member banks at the implicit charge of having their reserve balances earn no income. When the act made all types of depository institutions subject to reserve requirements, it necessitated that Federal Reserve payments services also be made available to them. Instead of maintaining the implicit fee system, the Congress determined that explicit charges should be made. The act thereby increased

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16. During this period, Board of Governors employment increased by almost 200. Total civilian employment in the executive branch decreased from 2,847,000 to 2,819,000. See Congressional Budget Office, Contracting Out for Federal Support Services: Potential Savings and Budgetary Impacts (October 1982).

17. Robert W. Hartman, Pay and Pensions, pp. 108-111.

the efficiency of the payments sytems by informing depository institutions of the resource cost of their activities and assessing them for these costs. 18/ The act also required that fees reflect actual Federal Reserve Bank expenses plus a return on capital that would be earned by and taxes paid by private business firms (the Private Sector Adjustment Factor, or PSAF). This markup prevents the Federal Reserve Banks from having an unfair pricing advantage over competing providers of payments services, the correspondent banks. The Federal Reserve was given the latitude to disregard the cost-plus markup rule if necessary to "give due regard to competitive factors and provision of an adequate level of such services nationwide." 19/

An additional benefit of the Monetary Control Act is that it may serve as a constraint on Federal Reserve Bank spending. If the costs of designated activities cannot be covered by revenue from customers, then the activities are to be reduced to bring costs into line with revenues or be discontinued. This market test is to be applied to any new payments services introduced by the Banks. This constraint on expenses could potentially also limit expenses in other service lines where costs are shared with payments services (buildings, for example).

Table 18 shows the 1983 expenses and revenue of the Federal Reserve Banks in the priced services area. Without taking the PSAF into account, the Federal Reserve Banks earned $47.5 million in profit, primarily in the check collection and wire transfer and net settlement services. With the PSAF taken into account, the Federal Reserve Banks took a loss of $11.6 million in the areas of check collection, definitive safekeeping and noncash collections (from a sharp volume reduction in safekeeping), commercial automated clearinghouse services, and cash transportation. The Board of Governors decided to provide subsidies in the latter two services. 1983 prices for commercial automated clearinghouse services were set to recover 40 percent of expenses plus the PSAF (resulting in a subsidy of $8.1 million);

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18. Total reserve balances were to decline under the act; in 1980, income from fees was projected to be approximately equal to the revenues forgone because of reduced earnings on reserves. See General Accounting Office, "The Federal Reserve Should Move Faster to Eliminate Subsidy of Check Clearing Operations" (May 7, 1982), pp. 53-57.

19. For an interpretation of the meaning of this clause, see Raymond Natter, Legislative Intent Regarding the Pricing of Services by the Federal Reserve Board, Congressional Research Service (January 25, 1984), p. 10.

TABLE 18. FEDERAL RESERVE BANKS: PRICED SERVICES EXPENSES AND REVENUE, 1983
(In millions of dollars)

	Commercial Check Collection	Wire Transfer and Net Settlement	Commercial Automated Clearinghouses	Definitive Safekeeping and Non-cash Collection	Book-entry Securities	Cash Transportation	Coin Wrapping	Total
Expenses	393.6	57.1	14.5	20.8	18.0	28.3	1.4	533.6
Private Sector Adjustment Factor (PSAF)	44.5	8.2	0.7	2.7	2.5	0.2	0.2	59.1
Expense Recovery Target	438.1	65.3	15.2	23.5	20.5	28.5	1.6	592.7
Revenue	436.7	67.2	7.7	19.1	21.8	27.1	1.6	581.1
Profit or Loss	-1.4	1.9	-7.5	-4.4	1.3	-1.4	0.	-11.6
Profit or Loss Excluding PSAF	43.1	10.1	-6.8	-1.7	3.8	-1.2	0.2	47.5

SOURCE: Board of Governors of the Federal Reserve System, Annual Report (1983), Table 9.

NOTE: Expenses reflect operating expenses, the cost of earnings credits, and--in the check collection service only--imputed float costs. Revenue reflects fees and income on clearing balances.

cash transportation subsidies ($1.6 million) were provided to remotely located depository institutions.

In 1982, priced services revenues were $90.9 million below expenses and the PSAF. The 1983 results show that the Federal Reserve has nearly met the revenue-cost matching requirement of the Monetary Control Act in the relatively short time period of three years. Spending on services for financial institutions and the public has risen by an average annual rate of 8.8 percent per year from 1979 to 1983, and has declined from 75.1 percent of total PACS-reported expenses to 65.7 percent (see Table 16).

Competitors of the System maintain that it has not fully complied with the act. 20/ They assert that the Federal Reserve has used its rule-making powers and guaranteed income to give itself a competitive advantage. Testimony of the American Bankers Association shows private-sector concerns about the market powers of the Federal Reserve.

> Any private sector competitor which operates on a nationwide basis, accounted for 40 percent of the market for its services, was twenty times the size of its next largest competitor, and engaged in the kind of "flexibility in pricing" described by the GAO report would be charged with price discrimination

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20. Lawrence C. Russell, "Testimony of the National Payments Coalition," in The Role of the Federal Reserve in Check Clearing and the Nation's Payment System, Joint Hearings before the Subcommittee on Domestic Monetary Policy of the House Committee on Banking, Finance and Urban Affairs and the Subcommittee on Commerce, Consumer and Monetary Affairs of the House Committee on Government Operations (June 15 and 16, 1983) and Barry F. Sullivan, "Statement on Behalf of the National Payments System Coalition," in Federal Reserve Pricing Policy on Check Clearing Services, Hearings before the Senate Committee on Banking, Housing and Urban Affairs (April 11, 1984). See also George C. White, "The Conflicting Roles of the Fed as a Regulator and as a Competitor," Journal of Bank Research, vol. 14 (Spring 1983), pp. 75-95. For a vigorous defense of the Federal Reserve's Monetary Control Act record, see the statement of Gerald E. Corrigan, President, Federal Reserve Bank of Minneapolis, in Federal Reserve Pricing Policy on Check Clearing Services," Hearings before the Senate Committee on Banking, Housing and Urban Affairs (April 11, 1984).

and almost certainly find itself in constant litigation with damaged competitors. 21/

These claims have been reviewed by GAO and by Committees of the House and Senate. A GAO study published in May 1982 found that the Federal Reserve needed to eliminate subsidies resulting from a decline in check-clearing volume, from a delay in pricing float, and from an intentional subsidy for commercial automated clearinghouse services. The decline in check-clearing volume, primarily the result of the establishment of explicit pricing, together with unexpected cost increases, caused commercial check collection to be subsidized at an annual rate of $40 million to $50 million in 1982. Price increases and service improvements have ended the subsidy of check-clearing services, according to a recent GAO report. 22/

In 1980, the Federal Reserve decided to reduce the level of float before pricing it at cost, arguing that the efficiency of the payments system could be improved by gradually changing its availability schedules and transportation system. The Government Operations Committee found in April 1984 that:

> . . . the Fed practice of giving better availability than it achieved, without including an appropriate charge in its fees, represented unfair competition. During this period the Fed should instead have increased its fees, in anticipation of completion of the operational improvements, by an estimated amount designed to prevent any unfair competitive advantage from its failure to charge fully for float, or, alternatively, the Fed should have adjusted its availability schedules to reflect more accurately the availability actually achieved. 23/

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21. Testimony of the American Bankers Association, "Federal Reserve System Pricing of Check Clearing Activities," in Federal Reserve Pricing Policy on Check Clearing Services, Hearings before the Senate Committee on Banking, Housing and Urban Affairs (April 11, 1984).

22. Government Accounting Office, "An Examination of Concerns Expressed About the Federal Reserve's Pricing of Check Clearing Activities" (January 14, 1985).

23. Federal Reserve Competition with the Private Sector in Check Clearing and Other Services, Report of the House Committee on Government Operations (April 11, 1984).

The Subcommittee on Domestic Monetary Policy of the House Banking Committee, on the other hand, has approved the Federal Reserve's policies. 24/ GAO estimates the revenue lost to the Federal Reserve to be $511.8 million for the period August 1981-August 1983 (inclusive). The subsidy for check collection float (the source of almost all float), was ended by the beginning of 1984, according to GAO.

The subsidy for the commercial activities of automated clearinghouses was also criticized by GAO in its 1982 report. The Federal Reserve maintained that the operations of these clearinghouses (by which transfers of funds may be made electronically in batch rather than by individual paper checks) were likely to show large economies of scale if they grew. In fact, the rates of growth of volume and cost have been similar through 1983. The GAO recommended that these automated clearinghouse subsidies be discontinued, or alternatively be capitalized and recovered through amortized interest payments by users after the end of incentive pricing. The Federal Reserve has not followed either of these recommendations; full recovery of costs is currently scheduled to occur in 1986. The April 1984 report of the House Committee on Government Operations criticized the System for continuing this subsidy.

FEDERAL RESERVE BUDGET SAVINGS APPROACHES

One purpose of subjecting the Federal Reserve to the appropriations process would be to realize savings in the Federal Reserve's budget. Savings are generally ordered through the appropriations process in two different ways. The first is the establishment of a ceiling on an agency's spending. Spending ceilings leave agency managers with the task of allocating spending reductions to different programs and objects of expense. The second way is the requirement of a reduction in spending for a particular purpose. These requirements may be explicit orders in appropriations riders or simply informal committee recommendations.

Both of these savings approaches may also be contained in authorizing legislation. It is more common, however, for authorizing legislation to order budgetary savings through major changes in the programs or structure of an agency. Authorizing legislation may require cost recovery for agency services, for example, or may reduce the size or responsibilities of an agency.

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24. The Role of the Federal Reserve System in the Nation's Check Clearing and Payments System (November 1984).

This section provides illustrations of how these savings approaches could be applied to the Federal Reserve, and discusses briefly the possible merits and drawbacks of the approaches.

Spending Ceilings

Banking Supervision and Regulation. An appropriations ceiling on supervision and regulation expenses is currently used for the Federal Home Loan Bank Board, but not for the National Credit Union Administration, the Comptroller of the Currency, Federal Deposit Insurance Corporation (FDIC), or the Federal Reserve. An argument against appropriations ceilings for these agencies is that they could be left without sufficient funds to promote the efficiency, equity, and safety of the banking system. If funds were limited to the degree that substantial delays in processing applications resulted, new financial services would not be available as early as possible, potentially reducing efficiency. A decline in spending on enforcement of consumer protection regulations could reduce access to credit for the disadvantaged. An inadequate level of supervision could lead to more problem banks and bank failures, with attendant public confidence, discount window, and financial insurance costs. On the other hand, the possibility of comparable mishaps has not deterred the Congress in appropriating funds for most of the other activities of the federal government. Other regulatory agencies are subject to the appropriations process, as is national defense. The FDIC insurance program and the Federal Reserve discount window loans offer some protection against short-term supervision problems.

Economic Policy. Most economic policy spending by the Federal Reserve is for preparation of statistics (such as monetary aggregates and flow of funds data) and policy analysis by the Board of Governors and the Federal Open Market Committee. An appropriations ceiling that constrained the Federal Reserve's flexibility to collect statistics and prepare analyses could leave it less well-informed. The Federal Reserve's research and statistics activities are extensive, a response in part to the uncertainty within the field of economics. As new policy problems confront the System, new or expanded surveys, statistical series, and analyses are commissioned. Over time, these studies may become less useful but be retained in the interest of preserving time-series data (that may once again become useful) or advancing basic research. Elimination of some of the less useful research and statistics activities could reduce spending while limiting the knowledge losses to System policymakers and other users. Potential savings in the statistical area may be bounded, however, by the Federal Reserve's record of reviewing and reducing its reporting requirements. This program began in 1975 and continued under the Paperwork Reduction Act of 1980. Because of its record of reducing paperwork burdens for the Information Collection

Budget, the Office of Management and Budget has delegated its authority for review of individual reports to the Board of Governors. It is the only agency to have received this delegation of authority.

Fiscal Agency and Financial Services. The Federal Reserve Act states that the Federal Reserve Banks, at the order of the Secretary of the Treasury, shall act as fiscal agents for the United States. 25/ The act does not require, however, that the Federal Reserve Banks receive full reimbursement for their costs. In 1983, the Federal Reserve received $72.9 million from the Treasury, the Department of Agriculture, and other government agencies in partial payment of total expenses of $120.3 million--a 60.6 percent reimbursement rate. Reimbursements came from the appropriated funds of these agencies, but Appropriations Committee review of the funds traditionally does not examine Federal Reserve Bank costs. The remaining $47.4 million was funded out of the Federal Reserve's income, decreasing the amount it would have returned to the Treasury. The Federal Reserve also bore the costs for certain services to financial institutions and the public to which the cost recovery requirement does not apply. These expenses totalled $176.7 million in 1983, 38.8 percent of net current expenses. Most of these expenses were for services with distinct governmental purposes—coin and currency processing and government and postal orders check processing.

Savings opportunities in the fiscal and financial services area are limited, for these expenses are largely mandatory in character—the government must distribute currency, pay its bills, collect taxes, and borrow money when necessary. The appropriations process could be used, however, to determine if the Federal Reserve's performance of these functions is cost-effective. Long-term cost reduction opportunities would largely depend on the feasibility of further automation of operations and subsequent reductions in personnel costs. Because most computer acquisitions do not reach their pay-back points for several years, a focus on limiting single-year expense growth (including the expense of computer purchases) could be myopic.

A possible problem with the use of the appropriations process in this area is the tendency of the Congress not to pass appropriations bills by the beginning of the fiscal year. It failed to pass 69 percent of the regular appropriations bills on time for fiscal years 1977-1983, relying on continuing resolutions to provide appropriations in their place. Such delays may force

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25. 12 U.S.C. 391.

agencies to follow inefficient spending practices. 26/ Basic Federal Reserve System operations would not be affected by this if the Federal Reserve was exempted from the provisions of the Anti-Deficiency Act (which prohibits spending until funds are provided by appropriations bills). The scope of the Anti-Deficiency Act is an unsettled legal issue, but some spending in the absence of appropriations is permitted under policy established by Office of Management and Budget memoranda. The policy allows agencies to continue only activities "that protect life and property and those necessary to begin phasedown of other activities." Defined to fall within this category are activities "essential to the preservation of essential elements of the money and banking system of the United States, including borrowing and tax collection activities of the Treasury." 27/

Specific Spending Reductions

In place of granting the Federal Reserve the choice of which programs or objects of expense to reduce in order to comply with a spending ceiling, the Congress could order specific spending reductions. For example, it could require that the Federal Reserve reduce its spending on regional economics. Many of the Banks have developed expertise in the economies and important industries of their districts, with staff economists serving as unpaid consultants to public and private task forces and as organizers of conferences. Such regional development and business analysis might be more appropriately performed by consortia funded by state governments and the private sector. On the other hand, if one accepts a federal interest in encouraging local economic development, regional research is a fit subject for the Federal Reserve Banks.

Another possible use of this approach would be to order the Federal Reserve to end immediately its subsidies for automated clearinghouses. These subsidies have been characterized as departures from the intent of the Monetary Control Act. So long as they are not prohibited, "Ready access to funds from the yield on Treasury securities the Federal Reserve owns makes a policy of subsidy easy to accomplish." 28/ On the other hand,

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26. General Accounting Office, "Funding Gaps Jeopardize Federal Government Operations" (March 3, 1981).

27. Office of Management and Budget, "Agency Operations in the Absence of Appropriations" (December 1982), pp. 1-2.

28. General Accounting Office, "The Federal Reserve Should Move Faster to Eliminate Subsidy of Check Clearing Operations" (May 7, 1982), p.34.

the Federal Reserve has stated that it will gradually terminate incentive pricing by 1986.

Cost Recovery and Privatization

Cost Recovery. Cost recovery for financial services has proved a significant source of budget savings for the Federal Reserve. The policy of cost recovery could be expanded by creating new user fees for certain of the System's public and service programs that are still financed from current income. These programs provide, for example, that the public can buy Treasury securities from the Federal Reserve Banks without paying sales commissions, free accounting assistance to banks, and free publications. Beneficiaries of these expenditures can be identified and may be willing to pay for them.

Another method of increasing cost recoveries would be to charge holding companies and state member banks for the costs of applications, examinations, and general supervision. This is the general practice of other financial regulatory agencies. The Comptroller of the Currency fully covers its costs through a general assessment on national banks and specific fees for charters, mergers, and branching. The FDIC draws funds from its assessment of 0.083 of 1 percent on the deposit liabilities of insured institutions. The Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation charge fees to partially cover examination and supervision costs, funding the remainder from assessments on funds raised in the securities markets by the Federal Home Loan Banks. State banking authorities also charge assessments and fees. 29/

Adoption of cost recovery for supervision and regulation expenses could produce significant savings in the Federal Reserve's budget. The notion that an industry should be charged for being regulated by the government is not novel, but it is unusual. Some of the regulatory activities of the Federal Reserve do not provide direct benefits to member banks, such as

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29. In 25 states, charges are added to general revenues and are appropriated to state banking departments. Charges are occasionally higher than the expenses of state banking departments, providing funding for other state programs. In 22 other states, charges are deposited into a fund for use only for the expenses of the banking department, but are still subject to appropriations review. Three state banking departments are independent. Conference of State Bank Supervisors, A Profile of State-Chartered Banking (January 1984).

examinations to determine compliance with consumer protection regulations. Supervisory activities may, however, alert management to problems with the bank's financial condition. On the whole, current policy protects banks to an extraordinary degree from economic loss, by providing access to discount window funds, restricting entry by potential competitors, and supervising risk-taking by banks that hold other banks' funds. A policy of cost recovery for regulatory costs may be justified by these benefits.

An efficient assessment and fee schedule would reflect the marginal costs of supervision and regulation activities. The Comptroller of the Currency charges banks assessments on a declining percentage scale of total assets, reflecting the significant economies of scale in labor costs from examining large banks. The FDIC, on the other hand, covers its supervision and examination costs by drawing on its insurance premiums from all insured banks. This creates a cross-subsidy from national and state member banks to state nonmember banks. An incentive to state member banks to withdraw from System membership would thereby exist if the Federal Reserve were to recover its supervision and regulation costs. With the adoption of universal reserve requirements, such withdrawals no longer create a problem for monetary policy control. Nevertheless, they could be retarded by separating FDIC insurance and examination costs and charging explicit fees for examination of state nonmember banks.

State member banks often are examined by the Federal Reserve and by their state supervisors in the same year, and could be charged twice if the Federal Reserve adopted cost recovery charges. In some states, state assessments and fees match or exceed those of the Comptroller, particularly for the larger banks. The desire to avoid dual charges could induce state-chartered banks to convert to national charters, which are already attractive because of the enhanced banking powers they provide in many states. They would also benefit from reduced compliance costs. It might be argued that the Federal Reserve should not charge fees for its supervisory activities in order to prevent mass conversions and preserve the traditional "dual banking system." This implies that the federal purpose in supervision and regulation of state-chartered banks is not clear. If a clear federal purpose is accepted, fees could be charged and consideration given to methods of reducing regulatory burdens from independent supervision. Substantial cost savings could be gained by having state and federal supervisors conduct annual exams on an alternating basis, or together. 30/

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30. Randall J. Miller, "Examination Man-Hour Cost for Independent, Joint, and Divided Examination Programs," Journal of Bank Research (Spring 1980), pp. 28-35. In 1983, 19 states participated in cooperative examination programs with the Federal Reserve.

Privatization. The Federal Reserve occupies a unique position in the payments system as the largest provider of services and as a regulator of its competitors. The potential conflict between these roles is a matter of concern, especially to its competitors. Also of concern is the provision and marketing by a government agency of services that may not be essential public services. One method of allaying these concerns would be to spin off the payments services of the Federal Reserve into a privatized enterprise. Although this approach would reduce government competition with the private sector, it would also result in the loss of the substantial joint economies from combining payments services and monetary policy activities in the same facilities, particularly from settlement and reserve account uses of the electronic communications system and account balances. It should be noted that the Federal Reserve has to an extent separated its priced services activities from its other activities.

Restructuring the Federal Reserve

The decentralized structure of the Federal Reserve System has remained relatively unchanged throughout its 70-year history. This has required the maintenance by each Federal Reserve Bank of separate overhead and support operations that would likely be centralized in a federal agency. Certain overhead and support costs--personnel services, for example--could obviously be reduced if Federal Reserve Bank operations were consolidated.

In the economic policy sphere, a recurrent recommendation has been that the Federal Reserve Bank presidents be dropped from the Federal Open Market Committee, on the ground that their voting status constitutes improper private-sector involvement in government policymaking. 31/ Their participation is also held to be unnecessary since the research staffs that support the Bank presidents independently prepare information that is often similar in content to that prepared by the Board of Governors staff. 32/

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31. Members of Congress have taken to court, unsuccessfully, to contest the absence of a requirement that Federal Reserve Bank presidents who are members of the Federal Open Market Committee be confirmed by the Senate. The courts held that the Members of Congress lacked standing. See Riegle v. Federal Open Market Committee, 656 F.2d 873 (D.C. Cir. 1981), cert. denied, 102 S.Ct. 636 (1981) and Reuss v. Balles, 584 F.2d 461 (D.C. Cir. 1978), cert. denied, 439 U.S. 997 (1978).

32. Henry S. Reuss, "The Once and Future Fed," Challenge, vol. 26 (March-April 1983), pp. 26-32.

Against this it is argued that the Bank presidents and their staffs provide regional perspectives and analytical diversity. At present the Board of Governors has several methods of controlling and coordinating Bank research, notably through its prepublication review of articles and through the System Research Advisory Committee composed of Board of Governors staff and Bank research directors.

Savings could also be made by consolidating the regulatory activities of the Federal Reserve, the Comptroller of the Currency, and the FDIC. The fragmentation among these agencies of responsibilities for federal regulation of commercial banks and bank holding companies has often been criticized. In the current system, one agency may have jurisdiction over a holding company while others have jurisdiction over the holding company's banks. The agencies have sometimes failed to share information and have duplicated each other's efforts. Separate annual surveys by the Federal Reserve System and the Comptroller of the Currency to determine pay levels for bank examiners provide an example of unnecessary overhead spending. Attempts by the agencies to coordinate activities and adopt uniform policies have had mixed success. 33/

Proposals to consolidate agencies have been made many times, most recently by the Grace Commission and the Bush Task Group. 34/ The Bush Task Group would create a Federal Banking Agency to regulate national banks and most holding companies. The Federal Reserve would have authority only for the largest holding companies and international banks, and initially be responsible for supervision of all state-chartered banks, leaving the FDIC free to concentrate on troubled banks. Over time, the Federal Reserve would divest its authority as primary supervisor of state-chartered banks to state supervisors when they were certified by the federal government. The Administration has not prepared estimates of the savings from

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33. General Accounting Office, "Federal Reserve Could Improve the Efficiency of Bank Holding Company Inspections" (August 18, 1981), and "Federal Financial Institutions Examination Council Has Made Limited Progress Toward Accomplishing Its Mission" (February 3, 1984).

34. President's Private Sector Survey on Cost Control, "Recommendations for Consolidation and Structural Changes in the Financial Service Regulatory Agencies," Report on Boards/Commissions—Banking and Investments (1983). Office of the Vice President, Blueprint for Reform: the Report of the Task Group on Regulation of Financial Services (1984). See also F. Jean Wells, Depository Financial Institutions: Regulatory Restructuring?, Congressional Research Service (August 14, 1984).

this plan. Any savings from consolidation would occur only over the long term, because of the significant transition costs of combining the agencies' personnel and operations. Whether states would bear the costs of supervision of state-chartered banks necessary for federal certification is uncertain.

THE APPROPRIATIONS PROCESS AND CONGRESSIONAL POLICY DIRECTION

Subjecting the Federal Reserve to the appropriations process would make possible increased Congressional direction of Federal Reserve policy. Control over the expenditures of the System could obviously give the Congress more influence on regulatory and monetary policies, because funding levels could be reduced if the Federal Reserve's goals or performance were deemed unsatisfactory. In addition, the annual regularity of the process would provide more opportunities to direct policy through riders than would use of authorizing legislation, which tends to be more sporadic.

The degree to which the Congress would use this additional power is unpredictable, as are the effects on policy. The Congress could use it to recapture the regulatory authority it has traditionally delegated to the Federal Reserve--for example, by attaching a rider to an appropriations bill that would direct the Federal Reserve, in the case of a certain set of banks, to classify loans as performing that it would otherwise classify as nonperforming. While similar limitations on the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corporation have not been used for this purpose, other regulatory agencies' policies have been affected by appropriations limitations. Whether the Congress should be making such decisions through the appropriations process is a highly controversial issue. Some see this as leading to political involvement in a technical area, while others see it as a legitimate exercise of Congressional policymaking authority. 35/

In the field of economic policy, the Congress could set appropriations ceilings on open-market, foreign currency, and discount loan transactions. This would be a significant change from current practice, in which the Federal Reserve has the authority to conduct its monetary transactions as it sees fit, and the ability to react to unexpected economic and financial

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35. Frederick M. Kaiser, Congressional Control of Executive Actions: Alternatives to the Legislative Veto, Congressional Research Service (December 12, 1983).

market conditions. If the Congress wishes the Federal Reserve to retain its operating flexibility yet still make it subject to the appropriations process, it could apply the process only to the System's administrative expenses, as it has done with the Treasury's Exchange Stabilization Fund transactions.

Even if the appropriations process was limited to administrative expenses, the Congress could still attempt to direct monetary policy through the use of riders or the withdrawal of funds. The Congress has attached monetary policy riders before. For example, Public Law 97-377, "Further Continuing Appropriations for Fiscal Year 1982," included the following:

> SEC. 161. . . . (I)t is the Sense of the Congress that: In recent months, the Board of Governors of the Federal Reserve and the Federal Open Market Committee have made a significant contribution to the lower interest rates without rekindling inflation, and that, with due regard for controlling inflation so as not to have an opposite effect of driving interest rates upward, they should continue to take such actions as are necessary to achieve and maintain a level of interest rates low enough to generate significant economic growth and thereby reduce the current intolerable level of unemployment.

This particular rider was a "sense of the Congress" rider that merely expressed the opinion of Congress. The usual appropriations rider, on the other hand, would have the force of law.

It is conceivable that Congressional control over the Federal Reserve's administrative expenses would not make a great deal of difference in the System's responsiveness to Congressional desires. Several empirical studies have found that the Federal Reserve has been generally responsive to the policy goals of the Congress and the President during the post-World War II period. It is possible, therefore, that the use of appropriations limitations would not substantially affect the direction of monetary policy.

Were the Congress to use riders to direct monetary policy, it would be explicitly determining monetary policy goals (targets for interest rates and/or money growth). To successfully discharge this enhanced responsibility, the Congress would need to set clear monetary policy goals that were achievable and consistent with other economic goals. It would also need to be able to interpret the very technical and often uncertain relationships between monetary policy instruments and economic conditions in order to monitor the Federal Reserve's conduct of monetary policy. These tasks would add significantly to the Congressional workload.

Use of the appropriations process might not be the most effective way of controlling monetary policy. The focus of the appropriations process is, after all, control of expenditures. Moreover, waivers of rules prohibiting legislation on appropriations would be necessary. If the Congress decided to reduce the traditional independence of the Federal Reserve and play a more active role in the formulation of monetary policy, a more effective means than the appropriations process would be the regular authorizing process of holding hearings and marking up, debating, and voting on substantive legislation. Conceivably, this could be integrated into the planning process established by the Congressional Budget Act of 1974 and the Full Employment and Balanced Growth Act of 1978. But it must again be emphasized that such a change would be a significant departure from current practice, requiring that the Congress develop a greatly expanded capacity for setting economic goals and for analyzing the relationship between the instruments of monetary policy and economic variables.

APPENDIX A. BUDGET PRESENTATION COMPARISONS

This appendix provides some comparative information about other organizations that share the Federal Reserve's off-budget status, and about the budget treatment of organizations that have activities similar to those of the Federal Reserve.

Other Off-Budget Organizations

Federal Reserve System spending is not the only spending excluded from on-budget outlays. Off-budget federal entities and government-sponsored enterprises are also excluded (see Table A-1). The former are agencies wholly or partially owned by the federal government, the receipts and expenditures of which have been excluded from the budget by statute or Presidential direction. The latter are enterprises not owned by the government although they were chartered by it and are sponsored by a federal agency; they are generally privately financed. The finances of all off-budget entities and government-sponsored enterprises are summarized in "annexed" budget schedules in the Budget Appendix.

The principal justification given by the 1967 President's Commission on Budget Concepts for excluding government-sponsored enterprises from the budget is their private ownership. All of the government-sponsored enterprises were privatized before the adoption of the unified budget, with the exception of the Student Loan Marketing Association. 1/

Off-budget federal entities have been excluded from the budget for a variety of reasons. In most instances, off-budget status was granted by statute to protect agencies or programs from budget reductions. This was the purpose of a provision of Public Law 98-21, which removes the Old Age and Survivors, Disability, and Hospital Insurance Funds of the Social Security Program from the budget beginning in fiscal year 1993. The Federal Financing Bank was excluded from the budget originally because it was intended to serve as a passthrough financing mechanism for agency debt. At present, however, the Federal Financing Bank also provides off-budget

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1. A Congressional Budget Office study of the budgetary status of government-sponsored enterprises is forthcoming.

TABLE A-1. OFF-BUDGET FEDERAL ENTITIES AND GOVERNMENT-SPONSORED ENTERPRISES, FISCAL YEAR 1985

Organization	Authority for Exclusion from the Budget
Federal Entities	
Rural Electrification and Telephone Revolving Fund; Rural Telephone Bank	Public Law 93-32
Board of Governors, Federal Reserve System	Presidential direction
Strategic Petroleum Reserve	Public Law 97-35
Federal Financing Bank	Public Law 93-224
Postal Service	Presidential direction
United States Railway Association	Public Law 93-236; Public Law 94-210
United States Synthetic Fuels Corporation	Public Law 96-294
Government-Sponsored Enterprises	
Student Loan Marketing Association	Presidential direction
Federal National Mortgage Association	Presidential direction
Banks for Cooperatives	Presidential direction
Federal Intermediate Credit Banks	Presidential direction
Federal Land Banks	Presidential direction
Federal Home Loan Banks	Presidential direction
Federal Home Loan Mortgage Corporation	Presidential direction
Federal Reserve Banks [a]	Presidential direction

[a] Federal Reserve Banks are not included in the Budget Appendix as either off-budget federal entities or as government-sponsored enterprises.

financing with the effect of reducing reported on-budget activities. 2/ Other agencies and programs--the Export-Import Bank, the Housing for the Elderly and Handicapped Fund, the Exchange Stabilization Fund, and the Pension Benefit Guaranty Corporation--have been at different times excluded from and included in the unified budget. 3/

Budget Presentation for Organizations with Similar Activities

Although many of the activities of the Federal Reserve System are similar to those performed by other federal agencies, the power and scope of Federal Reserve monetary policy activities is unique. Only the Exchange Stabilization Fund makes similar monetary policy transactions. Most of the organizations with activities similar to the other activities of the Federal Reserve System are included in the budget, as shown in the first column of Table A-2. This table also shows the means of financing for these organizations and records variances from executive agency status. The typical executive agency is headed by a single executive nominated by the President and confirmed by the Senate, is government-owned, and receives policy direction from the President. Variances from this status are multimember executives (commissions), executive members selected by private shareholders, and legal independence from Presidential policy direction.

All of the agencies having responsibilities in the fields of economic policy or economic statistics and research are dependent upon annual appropriations for financing. Depository institution regulatory agencies, on the other hand, are financed from nonfederal sources, and only the Federal Home Loan Bank Board and the Farm Credit Administration have their operating expenses limited by appropriations bills. Two other financial regulatory agencies, the Securities and Exchange Commission and the Federal Trade Commission, are subject to the appropriations process, as are three of

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2. Congressional Budget Office, The Federal Financing Bank and the Budgetary Treatment of Federal Credit Activities (January 1982); New Approaches to the Budgetary Treatment of Federal Credit Assistance (March 1984); James T. Bennett and Thomas J. DiLorenzo, "The Limitation of Spending Limitations: Off-Budget Activities and the Federal Government," Federal Reserve Bank of Atlanta Economic Review (April 1983), pp. 23-34.

3. Congressional Budget Office, An Analysis of Congressional Budget Estimates for Fiscal Years 1980-1982 (June 1984), pp. 59, 62.

TABLE A-2. CHARACTERISTICS OF ORGANIZATIONS WITH ACTIVITIES SIMILAR TO THOSE OF THE FEDERAL RESERVE SYSTEM

Activity and Organization	Budget Status (Fund Type)	Financing		Variances from Executive Agency Status
		Appropriations	Other	
Federal Reserve				
Board of Governors	Off-budget	No	Assessments on Federal Reserve Banks	7 members; independent a/
Federal Reserve Banks	Off-budget	No	Interest, fees and reimbursement for services	9 members each bank, selected by private shareholders and Board of Governors; independent
Monetary Transactions				
Exchange Stabilization Fund	On-budget b/ (Public Enterprise Fund)	Administrative expenses only	Interest/foreign exchange gains	None
Economic Policy				
Council of Economic Advisers	On-budget (Federal Fund)	Annual	None	None
Office of Management and Budget	On-budget (Federal Fund)	Annual	None	None
Office of the Secretary of the Treasury	On-budget (Federal Fund)	Annual	None	None

(Continued)

a. An agency is classified as "independent" if its executives cannot be removed from office by the President.

b. Administrative expenses, interest on Treasury securities, and foreign exchange gains and losses only.

TABLE A-2. (Continued)

Activity and Organization	Budget Status (Fund Type)	Financing		Variances from Executive Agency Status
		Appropriations	Other	
Economic Statistics and Research				
Department of Commerce Economic and Statistical Analysis	On-budget (Federal Fund)	Annual	None	None
Department of Labor Bureau of Labor Statistics	On-budget (Federal Fund)	Annual	None	None
Financial Regulation, Insurance, and Intermediation				
Comptroller of the Currency	On-budget (Trust Revolving Fund)	No	Assessments; fees from examinations	None c/
Federal Deposit Insurance Corporation	On-budget (Trust Revolving Fund)	No	Insurance fees; $3 billion in Treasury borrowing authority	3 members; d/ independent
Federal Home Loan Bank Board	On-budget (Public Enterprise Fund)	Limitation	Fees from; examinations; assessments on FSLIC & FHLBs. e/	5 members; independent

(Continued)

c. Five-year term, can be removed by President with notification to Senate.

d. One member must be the Comptroller of the Currency.

e. Federal Savings and Loan Insurance Corporation and Federal Home Loan Banks.

TABLE A-2. (Continued)

Activity and Organization	Budget Status (Fund Type)	Financing		Variances from Executive Agency Status
		Appropriations	Other	
Federal Home Loan Banks	Off-budget (Government-sponsored enterprise)	No	Debt issues; $4 billion in Treasury borrowing authority	14 members selected by private shareholders and by FHLBB; f/ independent
Federal Savings and Loan Insurance Corporation	On-budget (Public Enterprise Fund)	No	$750 million in Treasury borrowing authority	Under supervision of FHLBB; independent
National Credit Union Administration	On-budget (Public Enterprise Fund)	No	$100 million in Treasury borrowing authority	3 members; independent
Farm Credit Administration	On-budget (Federal Fund)	Limitation	Assessments	13 members; independent
Securities and Exchange Commission	On-budget (Federal Fund)	Annual	$1 billion in Treasury borrowing authority	5 members
Federal Trade Commission	On-budget (Federal Fund)	Annual	None	5 members; independent

(Continued)

f. The Banks were owned by the government until their capitalization was repaid by member institutions.

TABLE A-2. (Continued)

Activity and Organization	Budget Status (Fund Type)	Financing		Variances from Executive Agency Status
		Appropriations	Other	
Financial Services				
Bureau of Engraving and Printing	On-budget (Revolving Fund)	No	Reimbursements from Federal Reserve Banks and Postal Service	None
Bureau of Government Financial Operations	On-budget (Federal Fund)	Annual	None	None
Bureau of Public Debt	On-budget (Federal Fund)	Annual	None	None
Bureau of the Mint	On-budget (Federal Fund)	Annual	None	None
Postal Service	Off-budget g/ (Public Enterprise Fund)	Annual for 2 subsidies only g/	Collections; $10 billion in public and Treasury borrowing authority	11 members; independent

g. Payments to the Postal Service Fund (Federal Fund) are on-budget. These payments are for unfunded liabilities of the Post Office Department and for free and reduced-rate mail.

four Treasury Department bureaus with financial services functions. The fourth, the Bureau of Engraving and Printing, receives its financing from Federal Reserve and Postal Service reimbursements. All of these agencies are on-budget.

Three other organizations shown in Table A-2 are wholly or partially off-budget. The Federal Home Loan Banks are privately owned financial intermediaries for savings and loans. The Federal Home Loan Banks are supervised by the Federal Home Loan Bank Board, but do not carry out activities similar to the economic policymaking and regulatory activities of the Federal Reserve Banks. The Exchange Stabilization Fund budget statement includes interest earnings as offsetting collections and administrative expenses as obligations. The Fund's assets (securities, cash, and Special Drawing Rights) available for currency exchanges are shown as unobligated balances. Changes in foreign currency holdings are counted as outlays only when there is a realized loss on currency exchanges and as offsetting collections only when there is a realized profit. The Postal Service is excluded from the budget except for two subsidy payments to it funded by appropriations.

APPENDIX B. BUDGETING IN THE FEDERAL RESERVE SYSTEM

The System prepares separate budgets for the Board of Governors (under the direction of the Controller) and the Federal Reserve Banks (under the direction of the Division of Federal Reserve Bank Operations). Budget preparation proceeds on parallel tracks, however, with final approval by the Board of Governors in December. The Federal Reserve System's budget year is the calendar year, not the October 1-September 30 fiscal year of the federal government. Operating budgets are not prepared for discount loan activities and for securities and foreign currency transactions, which are conducted with regard to monetary policy goals only.

The Federal Reserve Banks. In the Federal Reserve Banks, budget preparation begins with the establishment in mid-spring of a target for spending growth for the budget year. The budget objective is prepared initially by the Conferences of First Vice Presidents and of Presidents in conjunction with the staff of the Division of Federal Reserve Bank Operations. After approval of the objective by the Board of Governors, the individual banks prepare draft budgets in the summer. During the fall, these budgets are reviewed by the Committee on Federal Reserve Activities, a three-member committee of the Board of Governors. Final budget submission and approval occurs in November and December.

In comparison to the control of obligations that is the focus of federal agency budgeting, the emphasis in the Federal Reserve Banks' budget process is on targeting percentage rates of growth (or decline) in major operating expense categories and employment. The System relies upon data collected by the Planning and Control System (PACS), which allocates direct and support costs by object of expense to the numerous activities of the Banks. These costs are then matched with selected environmental and productivity statistics, allowing the Banks and the Division of Federal Reserve Bank Operations to evaluate the comparative efficiencies of the Banks. The operating expense budget is prepared for only the upcoming year, unlike the standard federal practice of using a three-year planning horizon.

A separate budget is prepared for major capital outlays. Complementing the capital budget are processes to plan for and acquire automation and communications equipment and buildings. Each construction project, for example, must be approved by the Division of Federal Reserve Bank Operations in six major stages of acquisition, and approval by the Board of Governors may be necessary in up to four stages, should certain dollar limits of authority to make capital outlays (delegated by the Board of Governors to the Federal Reserve Banks) be exceeded.

In addition, a "System Project" budget process considers projects carried out by "host" Banks for the benefit of all Banks (an example is the standardization of computer software). Although System projects are controlled by the Board of Governors, the costs of these projects are shared by all Banks, and must be approved unanimously by the Banks every year. Banks also adopt "Business Plans" for their priced services activities. A Business Plan sets a course for matching the costs of priced services with revenues, and contains analyses of conditions in the payments markets, evaluations of the Federal Reserve Bank's capabilities to compete in these markets, and descriptions of planned marketing and operating strategies. Because the support and overhead activities of the Banks are shared by priced services and central bank and Treasury services, the results of the Business Plan processes are integrated into the operating and capital budgets. Business plans are approved by the Pricing Policy Committee of the Board of Governors, and are not made available to the public or to competitors. Operating and capital budgets are also affected by projected reimbursements for fiscal agent services from the Bureau of the Public Debt and Bureau of Government Financial Operations in the Department of the Treasury and the Food and Nutrition Service in the Department of Agriculture. These agencies consult with the Division of Federal Reserve Bank Operations and the Banks to determine the level of fiscal agent services to be provided.

Budget execution is monitored through monthly and quarterly reviews of PACS expense reports and a formal midsession review. In the priced services area, the stated policy of the Federal Reserve System is to respond to revenue changes with matched volume adjustments during the budget year, thereby changing the operating expense budget.

The Board of Governors. Preparation of the budget of the Board of Governors follows a similar, but compressed, timetable. Capital and operating expenses are integrated. Board expenses are budgeted for percentage rates of growth and personnel slots by division and by object of expense, and are not complicated by the reimbursement and priced services considerations faced by the Banks. The Board also prepares a currency budget, determining the amount of new currency to be produced by the Bureau of Engraving and Printing and reimbursed for by the Federal Reserve Banks. Monthly estimates of projected spending and the actual net financial condition of the Board are used to determine the semiannual assessments on Federal Reserve Bank earnings to cover Board of Governors expenses. The Federal Reserve Banks make quarterly payments to an account in the

Federal Reserve Bank of Richmond; these amounts are invested until drawn down by the Board of Governors.

Summary. Substantial differences exist between the budget processes used by the Federal Reserve and most federal agencies, especially the former's use of cost-based budgeting, decentralization, and capital planning. It is not uncommon for federal agencies to be criticized for overemphasis on control of obligations, disregard of field managers, and failure to analyze costs fully over the long term. Use of a budget process similar to that practiced by the Federal Reserve could reduce these problems. On the other hand, a drawback of decentralization is that the System may tolerate duplicative Bank overhead costs, or cause the Banks to bear high costs for coordination. The Federal Reserve's cost-based budgeting and decentralized spending authority could also complicate efforts by the Congress and agency executives to set binding limits on operating expenditures.

Representative **Hamilton**. Thank you very much, Mr. Penner.

You state accurately in your statement that the purpose of the proposed legislation is not intended to modify—as you put it—the existing balance of authority over monetary policy. There is not any effort, I think, to reduce the independence of the Fed here, and we all recognize the risks that would be incurred if that independence were jeopardized.

At the same time, I must say it really does bother me that these enormous sums of money are handled by the Fed without any detailed explanation of how the funds are handled, and that just runs contrary to every basic principle, it seems to me, that exists in an open and democratic society.

I said in my opening statement that the same rules should apply to the Fed as apply to other Government agencies. No agency of the Government should be able to take in and spend billions of dollars without having its budget open to public view.

Would you comment on that statement generally?

Mr. **Penner**. I think you have stated one of the primary issues very well. It is not, however, like a lot of the other attempts to move activities off-budget in the sense that moving the Federal Reserve on-budget, using any of the devices that we mentioned, would not change the bottom line; that is to say, it would not change the measurement of the deficit itself.

So that while we get very concerned when there is a change in accounting practices, that actually changes the deficit. I should modify that slightly. You could redefine the Federal Reserve income to be "seigniorage" and therefore a means of financing. But assuming you did not do that but rather continued to regard it as miscellaneous receipts or deductions from that interest, the bottom line would not be changed. The other modifier is that, especially with regard to capital transactions, the accounting procedures used in the budget of the United States are unfortunately probably least suited to really seeing what is going on in an agency like the Federal Reserve compared with other agencies.

Given the very clear gains that you suggested from this, I think the basic issue is whether it is worth the cost or whether similar oversight can be achieved using other devices like intensive hearings of the sort that the Banking Committee used to carry on in the Senate.

It is a tough choice, though everything you say about actually recording the resources used by the Federal Reserve is indeed important.

Representative **Hamilton**. Maybe I look at this matter from a too one-sided point of view, but I really cannot see legitimate arguments to support the view that the Fed should not have to disclose the details of its budget.

Mr. **Penner**. Again, as is so often the case, the question is whether the gains from that are worth the costs, and there are some costs. That is not a choice on which we can make a recommendation. But that is the main issue. Clearly, as I say in my statement, such numbers would indeed be useful for oversight.

Representative **Hamilton**. Does the fact that the member banks own the stock of the 12 Federal Reserve Banks make the Federal

Reserve in your judgement a private organization that should only be accountable to stockholders?

Mr. PENNER. I think the most practical point in that respect is that since the late 1940's the Federal Reserve has been conveying its profits to the central treasury and, therefore, any expenditure by these organizations reduces the amount of moneys available for public uses. Given that practice, I think the technical status of these things as being privately owned is really not important.

Representative HAMILTON. Now, the Fed, of course, does publish its budget for the preceding calendar year in its annual report. I wonder if you could advise us what kind of information is included in the Fed's budget and then compare it, perhaps, with the kind of information that you would find in the budget of other government agencies with regard to the amount of information and the quality of information that is available to you.

Mr. PENNER. I think there are a number of differences. As I said in my statement, one of the main reasons for a consistent disclosure is so that one can judge the amount of resources used by this agency as opposed to other agencies. That ability is limited by the fact that the Federal Reserve does use both different accounting concepts and uses a different time period. Therefore, the accounts of the Federal Reserve are published on a calendar-year basis of the calendar year just completed so that you cannot get a sense of their expenditure plans for the next fiscal year.

Moreover, in its capital accounts—and this is not a criticism of the Fed because it uses generally accepted accounting practices—it uses practices more like those of a private firm. That is to say, its investments are capitalized and then depreciated, whereas in a government account those capital expenses are recorded on basically a cash-flow basis. Because of these conceptual differences, the numbers are not comparable with those, say, of the FDIC or one of the other agencies that is on-budget.

Representative HAMILTON. Concerning the bill that we are talking about here, which really calls for information from the Fed as to how it handles money, do you think that would interfere in any way with the conduct of monetary policy and the so-called "cherished independence" of the Fed?

Mr. PENNER. First of all, I think the bill as written and as I understand it—and I am not a lawyer—would leave a lot of room for negotiating between the Federal Reserve and OMB as to exactly what definitions to use and how the accounts should be displayed.

Again, as I said in my statement, I think it is a matter of degree. The very least interference with Federal Reserve operations would come from just recording their operating account. I mentioned that their capital transactions do potentially pose a problem in the sense that if one was not careful, a whole industry could develop on Wall Street trying to "read the tea leaves" as to what exactly the Federal Reserve planned in the way of monetary policy from printing those prospective numbers. But as I also said in my statement, it would be relatively easy to get around that if the Federal Reserve were to adopt some convention of extrapolating the past.

Representative HAMILTON. So, it is quite possible to move toward a much greater disclosure of the Fed's operating expenses and financial transactions without, in your judgment, jeopardizing the independence of the Fed.

Mr. PENNER. Obviously, it always depends on how the information is used, and I suppose the Federal Reserve has some concern that that information would be used to interfere more in their management than they want. But certainly, at the extreme, just the recording of the operating expenses would pose very, very minor risks indeed. At the other extreme, of course, the notion of actually appropriating for those expenses, which we discuss in our report, could be used to exert very detailed control.

Representative HAMILTON. I am not suggesting that we get into the business of appropriating the Fed's budget in any way, and I agree with you that that might very well jeopardize the independence of the Fed.

But I cannot see how an informational requirement would do so.

Now, what are the drawbacks from a budget point of view of the annual report which the Fed uses versus publishing the data with the budget of the U.S. Government?

Mr. PENNER. The drawback would be simply because both the time period and the accounting conventions used are both different.

Representative HAMILTON. The Fed's annual budget is not helpful to the public, to you as a budget official, as is the budget of the U.S. Government, is it, as far as revealing information and detail?

Mr. PENNER. It does reveal a lot of information, I do not think that is the key problem. The key problem is that that information is not directly comparable with the FDIC-type information or other regulatory agency-type information.

Representative HAMILTON. There is a great deal more detail, is there not, in the U.S. Government budget than there is in the annual report of the Fed?

Mr. PENNER. Well, sir, I do not think that is really true. I mean, you do get a lot of information out of the annual report of the Federal Reserve. It is just displayed differently. I think that is the more important point, not the level of detail. Moreover, as I mentioned, an important point is the difference in the time period. That information refers to the past as opposed to their plans for the future.

Representative HAMILTON. Can you use the information in the Fed's annual report to compare its spending behavior to comparable Government agencies using the annual Government budget?

Mr. PENNER. Not on some items like the capital outlays. You have to get separate information on that, which you can get, of course.

Representative HAMILTON. Does the Fed ever publish projections of its spending?

Mr. PENNER. I do not think it does; no, sir.

Representative HAMILTON. All right. Representative Snowe.

Representative SNOWE. Thank you, Mr. Chairman.

Mr. Penner, exactly how would the Federal Reserve's independence be endangered if Congress required it to be subject to the appropriations process?

Mr. PENNER. First, usually when the notion of appropriating their moneys is raised, it is raised in the context of doing that just for their operating expenses. But, there are problems of differentiating those expenses that are clearly related to their business-type activities and their regulatory-type activities from those that are associated with monetary policy.

I think that those people who feel strongly about maintaining Federal Reserve independence, however, worry most that the appropriations language itself would be used to actually legislate monetary policy through the use of appropriations, riders, and so on. We have seen that sort of rider more and more in appropriations dealing with all manner of things.

That is the main concern. But, of course, even aside from that, there is some concern that you could use appropriations simply to punish the Federal Reserve. If you did not like what they were doing, the Congress could voice its displeasure which is, of course, a very awkward way of trying to manage their monetary policy, even if it were firmly believed that the Federal Reserve should have less independence.

Representative **Snowe**. So, it is not only concerned about riders to the appropriations bill, but also the kind of information they would present, that would also jeopardize their independence.

Mr. **Penner**. I do not think that the last point is necessarily true if it were confined to the operating expenses.

If the Federal Reserve had to project in detail their capital transactions, which of course is what they use to influence the reserves and so on, that would be a different matter. That would be a problem.

Representative **Snowe**. Do we have any way of knowing whether or not they fully recover their costs?

Mr. **Penner**. That is something that has been watched very carefully and it has been studied by the GAO. I think the Fed has passed, as it were, those examinations. There have been some limited exceptions to that, but I think as a general matter they have done quite well.

Representative **Snowe**. Do they turn over any of their earnings to the Treasury; do you have that information?

Mr. **Penner**. Yes; creating money is a very profitable activity, and they do indeed have very large profits relative to their expenditures. We expect them to turn over about $18 billion in fiscal year 1985.

In 1983, and I have the exact numbers here, their net current expenses were only $1 billion and they transferred to the U.S. Treasury $14.5 billion. Thus, the amount of profit is enormous relative to the amount of expenditures.

Representative **Snowe**. How is that information received? Do we get the kinds of earnings they turn over on an annual basis?

Mr. **Penner**. First of all, both OMB and CBO project those earnings in advance, and then those earnings are conveyed periodically during the year. It is one thing that we do not do a bad job of projecting. Therefore, the actual outcome is usually quite close to what we speculate it will be.

Representative **Snowe**. Are there any other agencies that are sort of comparable to the Federal Reserve System?

Mr. PENNER. The Federal Reserve, of course, is the only agency that actually has the power to create money. So, that is an extraordinarily important difference.

On the other hand, it does have a lot of activities that are comparable with other agencies, primarily in the regulatory area. To that degree, it can be compared with the Comptroller of the Currency or the Federal Deposit Insurance Corporation.

In terms of setting overall economic policy, I suppose, it can be compared with the Council of Economic Advisers and other like groups. We make that sort of comparison in our more complete report.

Representative SNOWE. Thank you, Mr. Chairman. Mr. Penner, thank you.

Representative HAMILTON. Senator D'Amato.

Senator D'AMATO. Thank you, Mr. Chairman.

Mr. Penner, you said that the Federal Reserve does projections with respect to their earnings; do you do that with OMB?

Mr. PENNER. We do that separately, sir. We give our own projections to the Congress, and they give their views with the President's budget.

Senator D'AMATO. How have your projections and OMB's stacked up traditionally over the years?

How have the Fed's earnings stacked up against both your projections and those of OMB?

Mr. PENNER. I think we have been quite close; percentage differences are small; of course, we are talking about a lot of money so absolute differences can amount to several hundred millions of dollars.

Senator D'AMATO. That is with respect to your office?

Mr. PENNER. Yes, I think both CBO and OMB. We are very close. We use essentially the same techniques for making the projections.

Senator D'AMATO. Let me ask you this, how does the Fed do with respect to coming in with the budget? Do they let you have any idea of what they are going to spend?

Mr. PENNER. No, they do not present a budget per se.

Senator D'AMATO. I wonder how they stack up. How much do you estimate it would cost the Federal Reserve to comply with the same budgetary reporting requirements that other agencies have and should they do it?

Mr. PENNER. We have had considerable discussions with them as to the amount of money—the sheer accounting cost is what you are talking about here—that would cost. We never resolved that completely. I guess I would suggest that would be a good question for Chairman Volcker when he testifies on this subject. We could never nail that down exactly.

Senator D'AMATO. Do you have any idea how much their budget is annually?

Mr. PENNER. The total current expenditures of the Federal Reserve Banks is $1.1 billion; that amount was for 1983. They had current income of over $16 billion. As I said to Congresswoman Snowe, the income just overwhelms the operating outlays.

Senator D'AMATO. A couple more questions.

Mr. PENNER. As I said, it is very profitable to create money, but there are obvious limits on that on the other side.

Senator D'AMATO. And you project that to be about $18 billion?

Mr. PENNER. Yes, sir, for fiscal year 1985.

Senator D'AMATO. How do you arrive at the figure? Do you do that by consulting with them?

Mr. PENNER. No, we do not consult with the Federal Reserve on that. It is not an extremely difficult thing to estimate compared with some of the things we have to estimate. Basically, we try to make a judgment as to how many assets they will add to their portfolio in the interest of creating bank reserves consistent with the kind of policies that they have announced.

Although it varies from year to year, let me say it would run $13 or perhaps $15 billion. That is the order of magnitude of what they would acquire every year.

We also look at the portfolio of their assets, the distribution of maturities, and so forth. We have our own interest-rate projection. That is the Achilles' heel of this whole thing. The most difficult thing to project is actual interest rates. We then apply that.

Senator D'AMATO. Are you talking about what they charge their banks?

Mr. PENNER. That is of some relevance, yes, sir. But it is of relatively minor relevance. The more important thing is the interest rate that they earn on their portfolio of Government securities, which is immense. That is basically what they return to the U.S. Treasury.

Senator D'AMATO. Let me ask you this, what effect, if any, is there of raising or lowering the discount rate with respect to their budget?

Mr. PENNER. I believe it would be very minor. Of course, most increases in it would raise their income; most decreases would lower it.

Senator D'AMATO. Is that really true? Would the money supply increase so that if you have a lower interest rate it would offset the higher earnings?

Mr. PENNER. Maybe I misunderstand you, sir. I am sorry.

Senator D'AMATO. With respect to the Federal Reserve discount policies, do they have any effect with respect to their earnings?

Mr. PENNER. Yes.

Senator D'AMATO. The Fed has, I think, just announced a policy to lower interest rates to 10 percent.

Mr. PENNER. Right, in fact, the discount rate was lowered to 7½ percent.

Senator D'AMATO. What effect does that have on their earnings?

Mr. PENNER. It would tend to lower them, but it would be a very minor item. For example, referring again to the 1983 data, their total interest earnings on discount loans was $139 million.

Senator D'AMATO. That is a very minor point.

Mr. PENNER. That is a very minor point. Their earnings on their holdings of U.S. Government securities, on the other hand, was $15.2 billion. So, it is really one-tenth or so of their total operations.

Senator D'AMATO. Mr. Chairman, I have no further questions. Thank you, Mr. Penner.

Representative HAMILTON. Mr. Penner, does the Federal Reserve System pay their people according to the civil service scale, or do they set their own?

Mr. PENNER. They have their own scale, sir.

Representative HAMILTON. Do we know what it is?

Mr. PENNER. Yes. We have a lot of details on that.

Representative HAMILTON. Is that published, or is that something that they have just given to you?

Mr. PENNER. Certainly it has been given just to us. But I think they have discussed it openly when they used to have more intensive oversight hearings.

Representative HAMILTON. For example, we really would not know what the pay scale of the Federal Reserve is on the basis of what is required to be published by them under law.

Mr. PENNER. Not in terms of the information in the budget appendix; no, sir.

Representative HAMILTON. What we do know about them comes through their voluntary disclosure of these matters.

Mr. PENNER. Yes, and they have been very cooperative with us in terms of giving us that short of information.

Representative HAMILTON. Do you have the general feeling that the Federal Reserve employees receive benefits that are not available to other employees of the Federal Government?

Mr. PENNER. Yes, they do receive some.

Representative HAMILTON. Can you supply some of them?

Mr. PENNER. The most important one that occurs to me is the thrift plan that they can engage in and through which they can defer tax.

Representative HAMILTON. How does that work?

Mr. PENNER. I do not have the details of that, sir. But basically it means that they can have some sort of salary deduction, which is then invested. It is sort of like the 401-K plan in the private sector.

Representative HAMILTON. There is no matching.

Mr. PENNER. Yes.

Representative HAMILTON. There is matching?

Mr. PENNER. There is matching, yes, sir. It is 40 percent.

Representative HAMILTON. Now, one of our former colleagues, Congressman Wright Patman who, I guess, was not a particular favorite of the Federal Reserve, used to say that they would have very lavish Christmas parties, buy recreational equipment and symphony tickets, which might be forbidden at other agencies of Government.

Do you think the Fed engages in that kind of thing now?

Mr. PENNER. CBO is not an audit agency, so we have not gone into their "books" in fine detail. It is obvious that the rules are somewhat different. But overall we found no evidence. I mean, we could just look at the aggregates. As I said, we did not go into their detailed accounts at all. But just from the aggregates, there is nothing to suggest their expenditures are far out of line compared with people who do similar types of things.

Representative HAMILTON. On page 28 of your report on the budgetary status of the Federal Reserve System, there is a table, table 1, identifying expenses and earnings of the Federal Reserve Banks.

Now, that is the kind of disclosure, I take it, that we now get from the Fed; is that correct?

Mr. **Penner**. That is correct, sir.

Representative **Hamilton**. They lump salaries of roughly half a billion dollars there, but there is no breakdown of any kind. But that is now the extent of disclosure after the fact that we get from the Fed; is that correct?

Mr. **Penner**. That is right, sir.

Representative **Hamilton**. There is nothing more than that available. There is not any annex or anything that gives us a lot more detail.

Mr. **Penner**. You can request backup reports of various things if you wish.

Representative **Hamilton**. Who can, we can in the Congress?

Mr. **Penner**. Yes, sir.

Representative **Hamilton**. And you can, I presume, and the Budget Office.

Now, the study that you have shows also on that page that the Federal Reserve Banks paid $85.2 million in dividends to shareholders in 1983. What is the reason a member bank should hold shares in the Federal Reserve Banks, and why should the Fed pay dividends to them?

Mr. **Penner**. I think that goes back to the history of the institution. I think the notion was basically that the central banking activity was so vitally important that there should be a local, geographical distribution of interests in it. That is why we set up the system of a board of governors and the various regional banks. At that time, surplus was paid in and the dividends are the return on that.

Representative **Hamilton**. Is it really that, is it a historical anachronism?

Mr. **Penner**. I do not think I would call it that, sir. I think there is still a strong feeling that the regional nature of the structure of the system is very important and that different regions of the country should be able to put in their opinions as to what the monetary policy should be.

As I understand it, the Congress takes fairly seriously the various requirements that serve that end—for example, the notion that there should be a geographical spread on the board of governors representing different regions in the country.

Representative **Hamilton**. Now, there is another item in there that is called transferred surplus, of $106.7 million, also on table 1, page 28.

What is the purpose of the Federal Reserve having a surplus and transferring it?

Mr. **Penner**. That is something I think that could be questioned more thoroughly. In an ordinary banking institution, obviously they want some sort of surplus to draw on in case they get an unexpected draw on their liabilities.

In the case of the Federal Reserve, however, the bottom line, as I said before, is that, it has the power to create money, and it has an immense quantity of assets. In short, it is extremely well covered and, therefore, one could question whether they need that sort of surplus.

Representative **Hamilton**. What do they do with that money, just put it in a kitty?

Mr. **Penner**. It is the equivalent of undistributed profits in a private firm.

Representative **Hamilton**. Do they make any accounting of it?

Mr. **Penner**. Do they make accounting of it?

Representative **Hamilton**. Yes. I mean, they have $106 million they transferred there last year. That is a nice little sum of money to have sitting around.

Mr. **Penner**. It is part of their equity, if you like, and it goes against the asset side of the accounts. In essence, you could say it is used to acquire assets. That is one way to look at it, just as in a private firm.

Representative **Hamilton**. What do they do with it?

Mr. **Penner**. It is a means of financing acquisition of assets, more government securities, discounting, and so forth. Again, it is the equivalent of equity in a private firm.

Representative **Hamilton**. Do they use it for other purposes? What kinds of legal restrictions are there? Suppose they want to throw a big party, can they use that money?

[Laughter.]

Mr. **Penner**. If they threw a big party, it would have the effect of reducing their overall profit level. It is a question of how they distribute their profits, or what they do with them. As I said, they conveyed in 1983 over $14 billion to the U.S. Treasury; some of it they just keep back to increase their equity. It has a counterpart on the asset side of the balance sheet—an acquisition of securities, or buildings, or what have you. It is what is left over after everything else. I think that is the point.

Representative **Hamilton**. Well, they could use that surplus to buy the stock back from its member banks; could they not?

Mr. **Penner**. Presumably they could do that, yes.

Representative **Hamilton**. Now, I want to explore how the money spent by the Fed for its administrative expenses affects the Federal budget and the Federal deficit. What impact does it have on the Federal budget?

Mr. **Penner**. Any extra dollars spent would have the effect of reducing the profit, if I can call it that, of the whole system and, therefore, would show up very probably as a reduction in the payment to the U.S. Treasury.

Representative **Hamilton**. So, there would be a reduction on the revenue side of the Federal budget.

Mr. **Penner**. The way we account for it right now, yes, sir.

Representative **Hamilton**. If you put the Federal Reserve on-budget, would that have any impact on the deficit figures?

Mr. **Penner**. There are a couple of ways you could do that. You could simply keep that payment in miscellaneous receipts where they are now, in which case it would have no effect on the budget deficit. The more usual approach of agencies like the Federal Reserve would be to consider that payment as a negative outlay rather than as a positive receipt. Again, that would have no effect on the budget deficit. A third way of doing it would be to say that this immense profit really comes from the creation of money and therefore in economist's jargon is a profit on the creation of money.

You could define that as a means of financing the deficit rather than as a reduction in the deficit. If you chose that approach, the deficit would rise as a result of it.

Representative **Hamilton**. Is it correct to say that measures which save money at the Fed reduce the Federal deficit?

Mr. **Penner**. That would be correct. The more efficiently they can do their jobs, the better off the deficit is.

Representative **Hamilton**. Representative Snowe.

Representative **Snowe**. Than you, Mr. Chairman.

Mr. Penner, how does the Federal Reserve System differ from other off-budget agencies in terms of reporting?

Mr. **Penner**. First of all, they do not project their expenditures and receipts out into the future. In their annual report and in the Board of Governors' section of the appendix, they talk about the past, about what they have done. They do not do it on a fiscal-year basis. Rather they do it on a calendar-year basis. They also use different accounting techniques. I do not mean to imply that their techniques are better or worse; they are just different.

In the Federal budget items we do things on a cash-flow basis. The Federal Reserve, with regard to its investments, do things more like an ordinary business would. That is, they capitalize their investments and then they depreciate them.

Representative **Snowe**. I see. So, they are on a calendar year rather than on a fiscal year.

Mr. **Penner**. Yes.

Representative **Snowe**. If we were to subject them to full disclosure of their operating budget, obviously they would have to change to a fiscal year. Would they also have to change their accounting procedures?

Mr. **Penner**. That is correct.

Representative **Snowe**. Does that require an awful lot? I mean, does that have enormous implications for them in any way?

Mr. **Penner**. It would be an expense, and it would not be a trivial expense. They would have to do a lot of computer reprograming and make a special effort. I assume that under those circumstances they would provide two sets of books as it were—one set using their traditional techniques for their private shareholders; another making their books comparable with those of other Government agencies.

Thus, it would be an expense. As I said, we have not been able to nail down a number to attach to that. As I also suggested, they may be able to do that by the time that Chairman Volcker testifies.

Representative **Snowe**. You referred to the GAO earlier. Is the GAO allowed to audit the Federal Reserve System in any way?

Mr. **Penner**. Yes; they are allowed to audit their operating activities. They are not allowed to get into critiques of monetary policy operations. But they are allowed to audit the Federal Reserve's regulatory and business-type activities, check clearing, and so forth.

Representative **Snowe**. Thank you, Mr. Penner.

Thank you, Mr. Chairman, I have no further questions.

Representative **Hamilton**. Let me just have you describe, if you would, in a little more detail how each of these options of your study would work.

You say in that study that there are three ways in which the Fed could be made more accountable:

One is making the Fed subject to the appropriations process.

The second is making more use of authorization legislation and the oversight process.

The third is publishing its budget along with the Budget of the United States.

Now, can you spell out for us how each of those options would work, with particular emphasis on the independence of the Fed.

Mr. **Penner**. I think everyone would agree that the first option is the most extreme with regard to independence. Again, most people who talk about that option talk about applying it only to the operating activities of the Federal Reserve and not to their actual open market activities. If you did the latter, you would be taking complete control over monetary policy down to the last detail.

But even as applied to their operating activities, that option could be used to discipline the Federal Reserve in various ways—for example, to punish them for bad behavior, attaching riders, and so forth. Obviously if you believe in the independence of the Federal Reserve, that would be the greatest threat to its independence.

With regard to more oversight through the authorization committees, that has been done in the past. I think the last time was 1980, when the Federal Reserve testified in great detail about its various operations, what they cost, how efficient they were, and so forth. That testimony was given before the Senate Banking Committee.

Oversight could be done, obviously, as often as the Congress wished. It would give the Congress an opportunity to look into great detail at the various expenditure items and so on. It would give Congress this opportunity without, again, passing any laws at least that would restrict the independence of the Federal Reserve in any way.

The third approach, which is the one we have been primarily talking about today, is simply a display of information—a display that puts the Federal Reserve on a comparable basis with other similar regulatory institutions. As I said, that approach would be purely informational, especially if it were just restricted to their operating-type activities.

In that regard, I suppose the Congress could see various aberrations or jumps in particular items, and that might draw their attention to items that would warrant a more intensive oversight proceeding of the type that I described.

Representative **Hamilton**. So, if your goal is to try to increase the accountability of the Fed for its spending, but to do that without interfering with the conduct of monetary policy, the latter option would best accomplish that—that is, the option of publication of the budget.

Mr. **Penner**. Yes. I think you can rank them as I did in the conclusion of my statement.

Representative **Hamilton**. Well, I would just like to make clear my own view.

I do not think that the Fed as a Government agency should have the freedom to take in and spend billions and billions of dollars without having its budget subject to some kind of public accountability.

I recognize the importance of the independence of the Fed and I do not want to intrude upon that independence. But I do not think the current procedure is adequate so far as giving the Congress and the public sufficient information about the operation of the Fed.

I do not mean to accuse the Fed of wasteful spending by my questions a few moments ago, I do not have any evidence of that at all. On the other hand, we draft laws in this country not on the basis of particular occupants of any agency or department at any one time, but we draft laws for permanent obligations.

So, I want to see the Fed maintain its independence, but I would also like to see it more accountable.

Your budget study, I might say, conducted by your office, has been exceedingly helpful to us. I think it was very well done.

Mr. PENNER. Thank you, sir.

Representative HAMILTON. We appreciate very much the work that you and your colleagues have done on it.

Now I would like to just ask a question or two about your thoughts on the current economy if I may—this is not the subject of the hearing.

But just released this morning was the first quarter estimate on the gross national product. You may have seen that. Are you familiar with that?

Mr. PENNER. Yes, sir. I have not been able to study it in detail, but I have the basic results in front of me.

Representative HAMILTON. I am sure that is true. The gross national product increased seven-tenths of 1 percent which is quite a bit under, is it not, the estimates that came out earlier?

Mr. PENNER. That is correct. The prior estimate was 1.3 percent.

Representative HAMILTON. Now, how do you construe this, what is its significance? We have seen reports in the paper that the stock market is booming, and we have also seen reports that the economists are saying—some economists are saying—that we are in for a period of stagnation if not recession.

It seems to me that we are at a fairly confusing time with regard to the course of the economy. I would like to get your judgment as to where we are.

Mr. PENNER. As you know, the quarterly numbers are really subject to a lot of random jumping around. A $4 billion difference in a $1.7 trillion real economy is equivalent to 1 percentage point annualized, the way we talk about those things. A recovery is bound to occur in fits and starts. On the other hand, there is no doubt that this is a disappointing number.

Our own view of the economy, however, does remain sanguine. We do believe that things will start to turn around. I think some of the numbers that you have seen recently have really been quite good. Housing looks like it is being stimulated; retail sales finally showed a little life last month. A big question mark is business capital formation. I think that is the thing that economists argue most about right now, other than about the trade deficit which is very important in all of this. But we are sanguine that the recent fall in interest rates will cause business capital formation to show some life. The bottom line of all of this is that I do not see any reason why our original February forecast—which was for fairly modest growth—will not be pretty close to the mark. That forecast for real growth during the four quarters of 1985 was 3.4 percent, and for 1986, 3.1 percent.

Representative HAMILTON. So you still hold to that.

Mr. PENNER. Yes, I think that will turn out to be a pretty good forecast.

Representative HAMILTON. And you do not agree with those economists now that are predicting we will slip into a recession sometime in 1986?

Mr. PENNER. I find that very hard to see, given the good fall we have had in interest rates. By my definition, the Federal Reserve's policy has been fairly loose recently and also, of course, we all know that fiscal policy, though detrimental in the long run, is quite stimulative in the short run.

Representative HAMILTON. Let me ask you this as the final question here. If the economy did stagnate or fall into a recession, the usual solution for that problem would be to stimualte through additional spending or a reduction of taxes on the fiscal side.

Is fiscal policy now removed, do you think, as an option that we could use in that case because of the very large deficits?

Mr. PENNER. I think it would be extremely difficult for a large number of reasons. First is simply the sheer size of the deficit, which makes one hesitate before applying traditional solutions.

Second, it has to be said that our budgeting procedures these days are very cumbersome. Therefore, it takes a long time to act.

Third, I think that there has been a fundamental change in the structure of the economy, which makes that sort of activity have a very weak impact these days. I think there is a psychological problem just from the fact of starting with a huge deficit and contemplating increasing it.

Beyond that—and more important, I think—is the fact that we live more and more each day in an international economy, and that is both with regard to the trade and goods and services, and with regard to capital flows. Indeed, I would suggest that at the short end, anyway, the international capital markets are almost perfect.

What happens when you try a traditional Keynesian-type stimulus—in our judgment—is that it immediately puts some pressure on our capital markets, starting to push real interest rates upward—real and nominal. Because these international capital markets are so perfect, that in turn starts to attract a lot of capital from them—much of which is American owned. I often slip into calling it "foreign owned." That is not proper, a lot of it is American owned.

In any case, it has the effect of increasing the value of the dollar, so you get an offset on the other side on the trade account which is contractionary, of course. Indeed, in pure economic theory, those two effects would offset each other exactly. I do not think the world works that perfectly.

But certainly the presence of flexible exchange rates and perfect international capital markets and, I would argue too, the growing sophistication of the way expectations are formed in the economy severely limit what you can do with fiscal policy.

Representative HAMILTON. And in that situation, then would you have to rely principally on monetary policy?

Mr. PENNER. Yes. The very features of the economy, that I described as reducing the power of fiscal policy, tend to enhance the power of monetary policy. In this international world if you increase the amount of liquidity in the economy and start to push down interest rates, you have a depreciating effect on the dollar and a natural increased stimulus, if you like, coming from the trade account.

Representative HAMILTON. Thank you very much, Mr. Penner, we are pleased to have you with us this morning and your very fine testimony. The subcommittee stands adjourned.

[Whereupon, at 11:10 a.m., the subcommittee adjourned, subject to the call of the Chair.]

THE BUDGETARY STATUS OF THE FEDERAL RESERVE SYSTEM

THURSDAY, JUNE 27, 1985

Congress of the United States,
Subcommittee on Economic Goals
and Intergovernmental Policy
of the Joint Economic Committee,
Washington, DC.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2257, Rayburn House Office Building, Hon. Lee H. Hamilton (chairman of the subcommittee) presiding.

Present: Representatives Hamilton, Scheuer, and Fiedler.

Also present: Charles H. Bradford, assistant director; and William R. Buechner and Joe Cobb, professional staff members.

OPENING STATEMENT OF REPRESENTATIVE HAMILTON, CHAIRMAN

Representative Hamilton. The subcommittee will come to order. We are very pleased to welcome Hon. Paul Volcker, Chairman of the Board of Governors of the Federal Reserve, to testify today on the budgetary status of the Federal Reserve System.

Each January the President submits a budget to Congress and the American people which gives the details of how the Federal Government proposes to spend the hundreds of billions of dollars it raises every year from the American taxpayer.

Full citizen access to the information in the Federal budget is an essential part of our democracy because this information helps voters judge how well the Government and its various components are carrying out their responsibilities.

There's one major Government agency, however, whose spending is not in the budget and that is the Federal Reserve System.

This omission weakens the usefulness of the budget. Let me quote from the testimony of Rudolph Penner, the Director of the Congressional Budget Office, who appeared during our first hearing on the budget status of the Federal Reserve:

> The current budgetary treatment of the Federal Reserve violates a basic principle of budgeting; namely, that the budget document should be comprehensive about Government operations and should facilitate cost comparisons among agencies and activities.

This omission of the Federal Reserve understates the amount of resources devoted by the Government to economic policy and bank regulation.

Last Friday, the Federal Reserve released its annual report for 1984. The report shows that the Federal Reserve System had total revenues of just over $18 billion in 1984, mostly from interest paid by the Treasury on the Fed's portfolio of U.S. Government securities. The Fed spent about $1.4 billion on its operating expenses and to print currency and returned just over $16 billion to the Treasury.

The only part of this to appear in the Federal budget is the amount returned to the Treasury, the $16 billion, which is included under the heading of "Miscellaneous Receipts."

In February, the Joint Economic Committee received a report from the Congressional Budget Office which listed three options for bringing the Federal Reserve into the budget process.

One option was to subject the Federal Reserve to the congressional appropriations process. The second was to increase the use of authorizing legislation and oversight. The third was to have the Federal Reserve publish its annual budget as part of the budget of the U.S. Government.

The CBO found that the first two options could be used by Congress to influence monetary policy. The third could not.

Recently I introduced a bill that would carry out the third option. The bill would put the revenues and expenditures of the Board of Governors and all the Federal Reserve banks into the Federal budget beginning in fiscal year 1987.

It would require the Fed to make some accounting changes and to make budget projections in order to give Congress and the public better information on its expenditures.

But the bill would not give Congress any additional control over the Fed's budget and would not interfere with the Federal Reserve's independence in setting monetary policy.

In January 1984, Chairman Volcker wrote me with the Fed's reasons for seeking to maintain its current budget independence. He said, in part:

> This budgetary autonomy has, I believe, been viewed by the Congress and others as an essential component of a structure designed to insulate the deliberations of the Federal Reserve from short term and partisan political pessures, while assuring that Federal Reserve policy remains responsive to the economic needs of the nation as a whole.

I recognize that the Federal Reserve has special responsibilities that may require it to take actions that are unpopular. Nonetheless, the same rule should apply to the Fed as applies to other Government agencies: No agency of the Government should be able to take in and spend billions of dollars without having its budget open to public view.

The Fed's need for a measure of independence from political pressures is not an excuse for shielding its budget from some process of accounting to Congress and the public.

[The bill referred to follows:]

99TH CONGRESS
1ST SESSION

H. R. 1659

To amend section 1105 of title 31, United States Code, relating to the President's budget to require it to separately set forth the annual budget of the Federal Reserve System.

IN THE HOUSE OF REPRESENTATIVES

MARCH 21, 1985

Mr. HAMILTON (for himself, Mr. COURTER, Mr. MITCHELL, Mr. BERMAN, Mr. BEDELL, Mrs. BOXER, Mr. FASCELL, Mr. FAZIO, Mr. HUGHES, Mr. LANTOS, Mr. MILLER of California, Mr. OLIN, Mr. RAHALL, Mr. ROE, Mr. ROSE, Mr. DENNY SMITH, Mr. SMITH of Florida, and Mr. VENTO) introduced the following bill; which was referred to the Committee on Government Operations

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A BILL

To amend section 1105 of title 31, United States Code, relating to the President's budget to require it to separately set forth the annual budget of the Federal Reserve System.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That section 1105 of title 31, United States Code, is amended by inserting at the end thereof the following new subsection:

"(f) The President shall submit with materials related to each budget transmitted under subsection (a) on or after January 1, 1986, a budget prepared by the Board of Governors of the Federal Reserve System, for itself and for all Federal Reserve banks, for the fiscal year for which the budget is submitted under such subsection and for each of the two fiscal years after that year. Each such budget shall include estimated receipts and expenditures of the Board of Governors of the Federal Reserve System and all Federal Reserve banks in the fiscal year for which the budget is submitted and the two fiscal years after that year.".

Representative HAMILTON. Chairman Volcker, we are delighted to have you with us. I have had an opportunity to read your prepared statement and I appreciate it. I especially appreciate the tone of it. And we will, of course, after your observations have a few questions for you. You may proceed.

STATEMENT OF HON. PAUL A. VOLCKER, CHAIRMAN, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

Mr. VOLCKER. Thank you, Mr. Chairman. I perhaps will read part of the prepared statement and summarize other parts, if that's satisfactory.

In any event, I appreciate the opportunity to appear before the subcommittee to discuss issues involved in the budgetary treatment and procedures of the Federal Reserve System. I have attached some rather lengthy appendexes to the prepared statement that I hope can be included in the record.

Representative HAMILTON. Without objection, Mr. Volcker, they shall be included.

Mr. VOLCKER. The appropriate budgetary treatment of the Federal Reserve has been considered a number of times. Each time Congress has examined the issue, it has concluded that the Federal Reserve's functional independence is inextricably intertwined with its budgetary independence. I believe the ability of the Federal Reserve, as provided by the Congress, to conduct its monetary policy with relative freedom from day-to-day political pressure has served the Nation well over the years. Maintaining the independence necessary to accomplish that objective should remain in the forefront of any consideration to change our budgetary treatment.

I realize, Mr. Chairman, that you are sensitive to those concerns. I understand that it is not your intent to propose that the Federal Reserve be subjected to the regular budget control processes of the administration or to congressional appropriations. Your concern, as I understand it, is to assure that adequate information is available to permit and encourage appropriate congressional review and public understanding of Federal Reserve spending.

In approaching that problem, we do share the common ground that the Federal Reserve is accountable to the Congress, and through the Congress ultimately to the American public, for its spending. The fact is we do make available substantial and detailed information on our spending and operations. Budgets for both the Board of Governors and the Reserve Banks are discussed and approved in open meetings of the Board. I would submit, in those respects, our accounts and budget process are already an "open book," as they should be.

Following my earlier discussions with you, Mr. Chairman, I have reviewed this matter in some detail and I would readily agree the "open book" is hard to read—sometimes confusing and enormously complex. I believe there are changes we can implement to make our budgets more conveniently accessible and more generally useful. For instance, with that objective in mind, this year's Annual Report of the Board of Governors to the Congress includes a chapter reviewing Federal Reserve spending over the last 10 years and our budget for 1985. We intend to present similar information in each annual report in the future.

The burden of my comments this morning is that the legitimate objectives of disclosure and public accountability can be best achieved by retaining independent budgetary reporting for the Federal Reserve (with our net earnings, as at present, reflected in the regular budget document). Integrating Federal Reserve expenditures into the Federal budget, contrary to our entire history and earlier congressional decisions, would, I fear, be interpreted as a clear step toward executive branch influence and control over the central bank. I am convinced that, in the end, the effect would be to make our operations less intelligible and "transparent" rather than more. At the same time, I believe we can better achieve your objectives by working with the Congress to improve procedures for reporting and oversight.

The next sections of my prepared statement, Mr. Chairman, review some of the history of our budgetary treatment and point out initially that it is not unique among treatment of central banks around the world. Indeed, it conforms broadly to the treatment in other countries generally; we have looked specifically at the major industrialized countries, and they all have comparable budgetary treatment to what we have.

You, I'm sure, understand and have indicated in your own statements that Congress has made a deliberate decision in the past to keep our budget outside the appropriations process and outside the executive review process precisely to maintain the independence of monetary policy decisions, and that broad philosophy and principle has been reviewed upon a number of occasions and, I think, confirmed and even reinforced through the years when it was considered.

Now I want to emphasize again that the aim of your bill is not to disturb the present method of Federal Reserve funding or expense control or to change the status of the System with Government, but my concern is that the proposed inclusion of Federal Reserve expenditures within the executive's budget document could be the first step down a slippery slope, encouraging those who clearly would wish to impair our functional independence by bringing the System more fully into the budgetary and appropriations process or by other means. And we do believe that the objectives you have can be reached more effectively and more cheaply by other approaches that are consistent with present procedures and budgetary treatment.

Now we do summarize in the prepared statement the existing budget process and the results within the Federal Reserve System. We try to make the point that we do have a very intensive planning and budgetary control process for both the Reserve Banks and the Board of Governors that has a number of steps which are detailed in the statement. The budgets are finally reviewed and adopted in open meetings of the Federal Reserve Board.

I have attached to my prepared statement a considerable amount of material that reflects the public reporting that we now do in detail on our expenditures, particularly in the so-called PACS report. My impression is that that material in detail and in speed of reporting is in excess of what any other Government agency provides. Maybe I'm wrong about that, but I have not seen any other Government agency that provides the same amount of detail with the same amount of speed and makes that available to the public; we do that in terms of expenditures for each Reserve Bank, each function of each Reserve Bank, each subfunction of the Reserve Banks throughout the Federal Reserve System.

If one looks at the overall results of our budgetary effort, I think we can take some satisfaction. Our real expenditures, expenditures in constant dollars, over the past 10 years has increased only 10.7 percent a year. Employment throughout the Federal Reserve System has been decreased by 13 percent over that decade. And all this took place while the principal measures of our workload, depending upon which function one takes, have increased from 50 to about 400 percent, all of which spells consistent and sizable increases in productivity.

We spend currently about $1.2 billion a year. Some $900 million of that reflects services to financial institutions, to the public, the Treasury, and Government agencies. In that area of the budget, we are largely reimbursed either by charging for our services or being reimbursed by the agencies for which we provide services.

A good many of our expenditures, about 40 percent of our expenditures, are for so-called priced services—clearing checks, wire transfers, coupon collections, and other services that we provide financial institutions. There, by law, we charge a price that fully recovers not only the cost of the service but imputed taxes and imputed profits to put us on a comparable basis with a private institution. And we are, in effect, in that area dealing in a competitive marketplace where there is a strong market incentive and pressure on our costs and expenditures simply to be able to charge a low enough price to remain in business.

These kinds of operational services—the priced services and the services we provide for other agencies for which we are reimbursed in whole or in part—are the major part, in sheer dollar volume, of our expenditures.

When we look at your bill, Mr. Chairman, I think we approach this from the standpoint that our budgeting does follow business accounting principles, including principally the depreciation of capital assets. Our budgets are also on a calendar year basis. I think that's less significant, but that is a difference from the way the Federal budget is presented, and we don't regularly make multiyear expenditure forecasts.

Your bill would require changes in that approach. All budget information would be provided in the same format and the same accounting conventions as used for on-budget agencies, and I take it the data would then, in your concept, be included in the Federal budget documents, although without provisions for executive branch review or congressional appropriations.

Some technical issues arise in that connection and they would have to be resolved if the bill were to be adopted, but I do not believe the results would effectively achieve the limited aims sought; that is, improved understanding and review of our expenditures by the Congress and the public.

The technical concerns arise from the differences in accounting procedures, the costs that would be involved with a changeover or with maintaining, which I think we would have to do, a dual accounting system, and the difficulties of forecasting Federal Reserve earnings several years ahead. Let me just say a few words on each of those.

We are a business-like organization. We basically keep our books as would a private concern. We follow generally accepted accounting principles, GAAP. The primary difference, as I said, is that we capitalize and depreciate major assets rather than expensing them in the year that they are acquired.

Indeed, I don't believe we could sensibly price our services on any other basis, given that the production of these services is highly capital intensive and that our prices, by law, must be set in a manner consistent with methods used by private sector providers of those services.

From the standpoint of budgetary management of both the Board of Governors and the Federal Reserve banks and the comprehensibility of those budgets to the public, GAAP accounting seems more sensible to me.

These problems implicit in Federal budgetary treatment could be overcome only by maintaining dual accounting systems, which would involve some sizable developmental and maintenance costs if done with precision. And I fear that two parallel accounting systems are more likely to contribute to confusion rather than clarity.

I might note in that connection, Mr. Chairman, that the approach that we use, particularly with depreciating assets, seems to me the one that's recommended by the accounting profession for organizations that must cost and price services, and we have that affirmed both by the General Accounting Office and by private accountants that we have consulted.

Your bill would require that the Federal Reserve forecast its revenues. The great bulk of the Federal Reserve's earnings are a byproduct of the implementation of monetary policy. Earnings on our portfolio of securities account for more than 95 percent of Federal Reserve receipts and reflect mostly the amount of currency outstanding, congressional and Federal Reserve decisions as to the level of reserve requirements, decisions on open market operations, and the level of interest rates. Meaningful forecasts of those variables are simply not feasible and would be liable to gross misinterpretation if considered indicative of future monetary policy.

Whatever those technical concerns, Mr. Chairman, my greatest concern is about the approach proposed in H.R. 1659 that transcends any technical considerations. We do plainly have the obligation to report to the Congress fully on our policies and operations. My sense is the arrangement for such reporting have, in most respects, worked relatively well over the years. As you know, as a matter of law, I testify four times each year before the Congress on the general conduct of monetary policy. Altogether, other Governors, Federal Reserve officials and myself appeared formally before the Congress on 34 occasions last year, and 34 times so far in 1985, testifying on a variety of subjects.

The question raised is whether, in this testimony, in other reports, or otherwise, there is enough focus on our "housekeeping" responsibilities—running an economical, cost-effective operation. Appropriate congressional oversight of the Federal Reserve spending can and should contribute to that process. I believe this can be done in a manner that does not raise questions about the independence of our budgetary processes and which contributes to public understanding.

To those ends, I would suggest:

Only within the Federal Reserve System, we take steps to assure that the mass of information now available in several documents about our spending and budgetary process be presented at times and in a manner more accessible to public and congressional oversight. We are taking steps in that direction, and would welcome further suggestions you may have as to how to make the process more useful.

Two, we retain our present accounting format, using GAAP concepts rather shifting to the Federal budget accounting conventions. My strong belief is that Federal Reserve spending is likely to receive more, and better informed, congressional and public scrutiny as part of a separate report consistent with GAAP accounting.

The net fiscal impact of Federal Reserve operations is already fully and accurately reported in the budget. Forcing the full array of supporting material into the dark recesses and precise format of a budget presentation developed for quite different purposes—a presentation that already runs to thousands of pages—could hardly be a service to public understanding. It would, suspect, become just another hard-to-understand "special analysis," alongside a number of others virtually incomprehensible to those untutored in the intricacies of budget accounting for government or government-sponsored enterprises.

Three, finally, the appropriate committees in the House and Senate might wish to resume a practice, followed for some years in the Senate, of annual hearings directed specifically toward the Federal Reserve budget and internal management. I believe we, as an organization, benefited from that procedure in the past, and would be glad to cooperate in the future.

In closing, Mr. Chairman, I appreciate the careful way in which you have undertaken a reexamination of these questions. Our goals are congruent—to achieve effective cost containment and appropriate accountability. I believe those aims can be accomplished in ways fully consistent with our traditional role in government, and without raising unintended questions about whether the conduct of monetary policy will continue to be free from partisan and passing political pressures. Thank you, Mr. Chairman.

[The prepared statement of Mr. Volcker, together with the attached appendixes referred to, follows:]

PREPARED STATEMENT OF HON. PAUL A. VOLCKER

I appreciate the opportunity to appear before this Committee to discuss issues involved in the budgetary treatment and procedures of the Federal Reserve System. Attached to my statement are several appendices which discuss these questions more completely. I request those materials be included in the record.

The appropriate budgetary treatment of the Federal Reserve has been considered a number of times. Each time Congress has examined the issue, it has concluded that the Federal Reserve's functional independence is inextricably intertwined with its budgetary independence. I believe the ability of the Federal Reserve, as provided by the Congress, to conduct its monetary policy with relative freedom from day-to-day political pressure has served the nation well over the years. Maintaining the independence necessary to accomplish that objective should remain in the forefront of any consideration to change our budgetary treatment.

I realize, Mr. Chairman, that you are sensitive to those concerns. I understand that it is not your intent to propose that the Federal Reserve be subjected to the regular budget control processes of the Administration or to Congressional appropriations. Your concern, as I understand it, is to assure adequate information is available to permit and encourage appropriate Congressional review and public understanding of Federal Reserve spending.

In approaching that problem, we share the common ground that the Federal Reserve is accountable to the Congress, and through the Congress ultimately to the American public, for its spending. The fact is we do make available substantial and detailed information on our spending and operations. Budgets for both the Board of Governors and the Reserve Banks are discussed and approved in open meetings of the Board. I would submit, in those respects, our accounts and budget process are already an "open book," as they should be.

Mr. Chairman, following my earlier discussions with you I have reviewed this matter in detail. I would readily agree the "open book" is hard to read -- sometimes confusing and enormously complex. I believe there are changes we can implement to make our budgets more conveniently accessible and more generally useful. For instance, with that objective in mind this year's Annual Report of the Board of Governors to the Congress includes a chapter reviewing Federal Reserve spending over the last ten years and our budgets for 1985. We intend to present similar information in each Annual Report in the future.

The burden of my comments this morning is that the legitimate objectives of disclosure and public accountability can be best achieved by retaining independent budgetary reporting for the Federal Reserve (with our net earnings, as at present, reflected in the regular budget document). Integrating Federal Reserve expenditures into the Federal Budget, contrary to our entire history and earlier Congressional decisions, would, I fear, be interpreted as a clear step toward Executive influence and control over the Central Bank. I am convinced that, in the end, the effect would be to make our operations less intelligible and "transparent" rather than more. At the same time, I believe we can better achieve your objectives by working with the Congress to improve procedures for reporting and oversight.

The Federal Reserve as a Self-Funding Central Bank

The Congress established a central bank for the United States much later in the nation's history than has been the case in most other industrialized countries. To a considerable extent this reflected long and strongly felt concerns about concentration of economic power. At the same time, the Congress clearly wished to insulate the Federal Reserve from partisan politics. These concerns led to the creation of a regional system, with operational responsibilities diffused among 12 Reserve Banks, each with its own board of directors and with the entire system supervised by the Board of Governors in Washington.

In that connection, Congress plainly understood that the ability to make considered monetary judgments, independent of day-to-day pressures of the political arena, required freedom from outside fiscal control. These concerns were also evident in the important revisions of the Federal Reserve Act in 1935, which cast the System in essentially the form it has today.

The desirability of independent funding of the Federal Reserve and freedom from potential domination by the Executive Branch has been reaffirmed each time questions have been raised. And it has not been a partisan or parochial position. For instance, in 1975 six former Secretaries of the Treasury, in a letter to Senator Proxmire, stressed how important they felt it was that the Federal Reserve retain its status as a nonappropriated agency in these words:

> "We all feel that the Congressional reasoning of 60 years ago which purposely insulated the Federal Reserve from immediate political pressures is even more valid today. It is probably more difficult today than 60 years ago for the Congress to take a long view that may well appear to conflict with immediate problems. And yet, this is precisely what the Federal Reserve must do each day and why we feel that its independence must be preserved.
>
> "We all agree from a combined total of many years of experience in government that the independence of the Federal Reserve would inexorably be eroded by the appropriations process exposing our country to great potential danger."[1]

I should also point out that the budgetary status of the Federal Reserve is hardly unique; it is indeed the norm for central banks around the world. For instance, whatever other arrangements surround their functional independence, all the central banks of the G-10 countries finance their expenditures out of their own income. Typically, they return all or major parts of their income in excess of expenses to the national treasury, as is the case in the United States, but in no instance is a budget statement for the central bank included in the budget for the central government. That approach by other major industrialized countries reflects widely held concerns about assuring operational autonomy for central banks. (Appendix B discusses financing of the Central Banks of other major countries in more detail.)

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[1] Federal Reserve Reform and Audit Hearings, 1975, hearings before the Senate Committee on Banking, Housing and Urban Affairs, on S. 2285; and S. 2509, 94th Congress (October 20, 1975), p. 140. (Appendix A discusses the history of Federal Reserve budgetary independence more fully.)

I recognize and appreciate that the stated aim of H.R. 1659 is not to disturb the present method of Federal Reserve funding or expense control, much less to change the status of the System within government. My concern, nonetheless, is that the proposed inclusion of Federal Reserve expenditures within the Executive's budget document could be the first step down a slippery slope, encouraging those who clearly would wish to impair our functional independence by bringing the System more fully into the budgetary and appropriation process or otherwise.

Federal Reserve System Budget

The objective specifically sought by H.R. 1659 can, in my judgment, be reached more effectively and more cheaply by other approaches consistent with present procedures and budgetary treatment. To help place this issue in context, I would like to summarize the existing budget process and results.

The Process

The Federal Reserve has an intensive planning budget and control process for both the Reserve Banks and the Board of Governors. That process reflects throughout strong concern with both economy and efficiency.

Initial general guidelines for System spending are approved by the Board of Governors on the basis of analyses and projections of expected workloads, trends in prices and wages, and productivity gains in each area of Federal Reserve responsibility. Within each of the Reserve Banks, Directors drawn from the private sector, participate in the budgetary process, bringing to bear a great deal of business experience. They must approve the budgets of their banks.

I would emphasize too that more than 40 percent of Reserve Bank budgets represent expenditures for "priced services". As a matter of law and principle, these services must meet a market test in that all expenses (including overhead, and the imputed cost of capital and taxes) are covered by charges.

As a last step, budgets for both the Reserve Banks and for the Federal Reserve Board operations are presented to the Board of Governors for its review and approval at meetings that are open to the public. (The internal review process is outlined in Appendix C.)

The Results

In the end, the effectiveness of the process must be measured by results. In the ten-year period from 1974 to 1984 Federal Reserve spending has increased at an average annual rate of about 0.7 percent in constant dollars (Chart 1). In the same period, total System employment has fallen by about 13 percent, from roughly 28,000 to 24,000 (Chart 2). Over the same decade, the principal measures of operational workload have increased by 50 to almost 400 percent (Table 1). The long-term decline in Federal Reserve employment in face of persistent increases in output reflect in large measure persistent efforts to improve productivity in the operating functions of the Federal Reserve Banks.

For 1985 the Federal Reserve Banks and the Board of Governors have budgeted total operating expenditures of approximately $1.2 billion.2/ Of this amount, some $900 million reflects operational services to financial institutions, the public, the Treasury and Government agencies, most of which is recovered by charges or reimbursements. Overall, this will represent an increase of about 5 percent, in nominal terms, over the 1984 spending level (Table 2).

2/ This does not include another $175 million which will be paid to the Bureau of Engraving and Printing for Federal Reserve notes to be distributed to the public. This sum is not usually included in analyses of Federal Reserve spending because it represents simply the cost of providing currency.

As I indicated a few moments ago, under the provisions of the Monetary Control Act, the System must recover the full cost of most services (including an adjustment for imputed taxes and the cost of capital) it makes available to depository institutions. In this area -- clearing checks, providing wire transfers, and other payments services -- the Federal Reserve effectively has to compete in terms of price and quality with other actual and potential suppliers of such services. In 1984 the Federal Reserve met this test and recovered the full cost of priced services.

As fiscal agent for the U. S. Government, the Federal Reserve is responsible for issuing and redeeming a variety of Treasury and other government debt instruments ranging from savings bonds and food stamps to large denomination Treasury bills, notes and bonds. We are reimbursed in whole or in part for these services by other agencies, bringing our receipts for services to more than $600 million this year, about half of total expected Federal Reserve expenditures budgeted for 1985.

While this may not be the time or place to review the spending record in great detail, I have attached relevant material in Appendix D and would, of course, be glad to respond to any questions you may have. But I do want to affirm that I believe that further analysis will confirm a disciplined budgetary process and a consistent pattern of economy and efficiency in our actual spending. Indeed I am not aware that our record in these respects has been challenged in any material before the Committee.

Information Now Publicly Available on Federal Reserve Spending

The Federal Reserve now makes available detailed information on its spending. Much of this data is drawn directly from the Federal Reserve's accounting and management information system (Planning and Control System, or "PACS") used for internal control. That system contains data on spending by every Reserve Bank and branch office by service and subservice line and by object of expenditure (i.e., salaries, materials and supplies, equipment, travel and others). All in all, the "PACS" reports provide data on 96 services and subservices by 71 detailed objects of expenditure, as well as productivity and service quality measures. These data are publicly available on a quarterly basis with a six-week time lag, and I know of no other governmental body that provides publicly so much detail about its spending and productivity so promptly.[3]

PACS information by its nature is retrospective. However, the Federal Reserve also makes available late in each year information in the form of tables and analyses of anticipated expenditures for the forthcoming year. These are released to the public prior to the open Board meetings at which spending levels for the Board and the Reserve Banks are set.

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[3] I have included with my statement a Summary PACS report for the first quarter of 1985 for your information.

Whether we have provided all available information in as readily convenient a form as possible is another question. I believe improvements can be made. We are working to that end.

Difficulties with the Approach of H.R. 1659

Our Federal Reserve budgeting generally follows business accounting principles, including depreciation of capital assets. The budgets are on a calendar year basis, and we do not regularly make multi-year expenditure forecasts.

H.R. 1659 would require changes in that approach. All budget information would be provided in the same format, and with the same accounting conventions, as used for "on budget" agencies. The data would then be included in the Federal budget documents, although without provisions for Executive Branch review or Congressional appropriations.

Technical issues, as well as fundamental philosophical concerns, would need to be resolved before such an approach could be adopted. And, I do not believe the results would effectively achieve the limited aims sought -- that is, improved understanding and review of our expenditures by the Congress or the public.

The technical concerns are threefold: first, problems arising from differences in the accounting procedures used by the Federal Reserve and those employed by budgeted agencies; second, the costs that would be associated with the necessity of maintaining a dual accounting system, and third, the difficulties of meaningfully forecasting Federal Reserve earnings several years ahead.

With respect to accounting conventions, the Federal Reserve is a "business-like" organization that basically keeps its books as would a private concern -- that is using generally accepted accounting principles (GAAP). The primary difference in approach from Federal budget concepts is that the Federal Reserve capitalizes and depreciates major assets rather than expensing them in the year that they are acquired.[4] Indeed, we could not sensibly price our services on any other basis, given that the production of these services is highly capital intensive and that our prices, by law, must be set in a manner consistent with methods used by private sector providers. Specifically, expensing computers and other equipment in the year acquired -- rather than following GAAP -- would result in widely fluctuating prices for Federal Reserve services, rendering the pricing approach stipulated by the Monetary Control Act practically impossible. More generally, from the standpoint of budgetary management of both the Board of Governors and the various Federal Reserve Banks -- and the comprehensibility of those budgets to the public -- GAAP accounting seems more sensible.

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[4] The GAAP approach used by the Federal Reserve is particularly recommended by the accounting profession for organizations that must cost and price products. See, for instance: Comptroller General of the United States, Report to the Chairman, Committee on Banking, Housing and Urban Affairs, United States Senate, "An Examination of Concerns Expressed about the Federal Reserve's Pricing of Check Clearing Activities;" and Arthur Andersen & Co., "Federal Reserve System: Report on Priced Services Activities," September 1984.

These problems implicit in Federal budgetary treatment could be overcome only by maintaining dual accounting systems, which would involve some sizable developmental and maintenance costs if done with precision. And, two parallel accounting systems are more likely to contribute to confusion than clarity.

H.R. 1659 also would require the Federal Reserve to forecast our revenues. The great bulk of the Federal Reserve's earnings are a by-product of the implementation of monetary policy. Earnings on our portfolio of securities account for more than 95 percent of Federal Reserve receipts and reflect mostly the amount of currency outstanding, Congressional and Federal Reserve decisions as to the level of reserve requirements, decisions on open market operations, and the level of interest rates. Meaningful forecasts of those variables are simply not feasible and would be liable to gross misinterpretation if considered indicative of future monetary policy. I would also point out that forecasts of costs and receipts in the priced services area would also be subject to market uncertainties, and necessarily be somewhat speculative.

Policy Concerns

My greatest concerns about the approach proposed in H.R. 1659 transcend these technical considerations.

We plainly have the obligation to report to the Congress fully on our policies and operations. My sense is the arrangements for such reporting have, in most respects, worked relatively well over the years. As you know, as a matter of law, I testify four times each year before the Congress on the general conduct of monetary policy. Altogether, other Governors, Federal Reserve officials and myself appeared formally before the Congress on 34 occasions last year, and 34 times so far in 1985, testifying on a variety of subjects.

The question raised is whether, in this testimony, in other reports, or otherwise, there is enough focus on our "housekeeping" responsibilities -- running an economical, cost-effective operation. Appropriate Congressional oversight of Federal Reserve spending can and should contribute to that process. I believe this can be done in a manner that does not raise questions about the independence of our budgetary processes and which contributes to public understanding.

To those ends, I would suggest:

1) Within the Federal Reserve, we take steps to assure that the mass of information now available in several documents about our spending and budgetary process be presented at times and in a manner more accessible to public and Congressional oversight. We are taking steps in that direction, and would welcome further suggestions you may have.

2) We retain our present accounting format, using GAAP concepts rather than shifting to the Federal budget accounting conventions. My strong belief is that Federal Reserve spending is likely to receive more, and better informed, Congressional and public scrutiny as part of a separate report consistent with GAAP accounting.

The net fiscal impact of Federal Reserve operations is already fully and accurately reported in the Budget. Forcing the full array of supporting material into the dark recesses and precise format of a budget presentation developed for quite different purposes -- a presentation that already runs to thousands of pages -- could hardly be a service to public understanding. It would, I suspect, become just another hard-to-understand "special analysis," alongside a number of others virtually incomprehensible to those untutored in the intricacies of budget accounting for government or government-sponsored enterprises.

3) Finally, the appropriate oversight committees in the House and Senate might wish to resume a practice, followed for some years in the Senate, of annual hearings directed specifically toward the Federal Reserve budget and internal management. I believe we, as an organization, benefitted from that procedure in the past, and would be glad to cooperate in the future.

In closing, Mr. Chairman, I appreciate the careful way in which you have undertaken a reexamination of these questions. Our goals are congruent -- to achieve effective cost containment and appropriate accountability. I believe those aims can be accomplished in ways fully consistent with our traditional role in Government, and without raising unintended questions about whether the conduct of monetary policy will continue to be free from partisan and passing political pressures.

* * * * * * * *

CHART 1

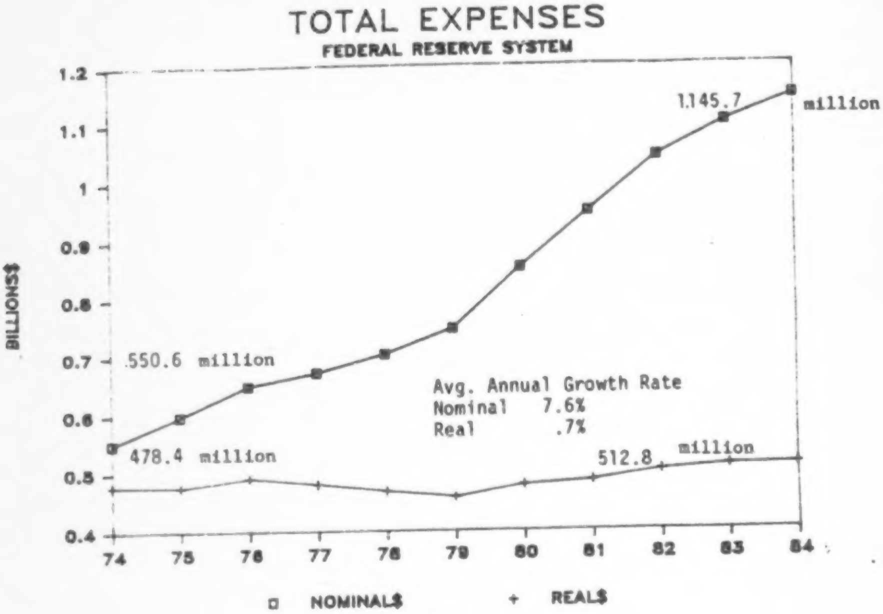
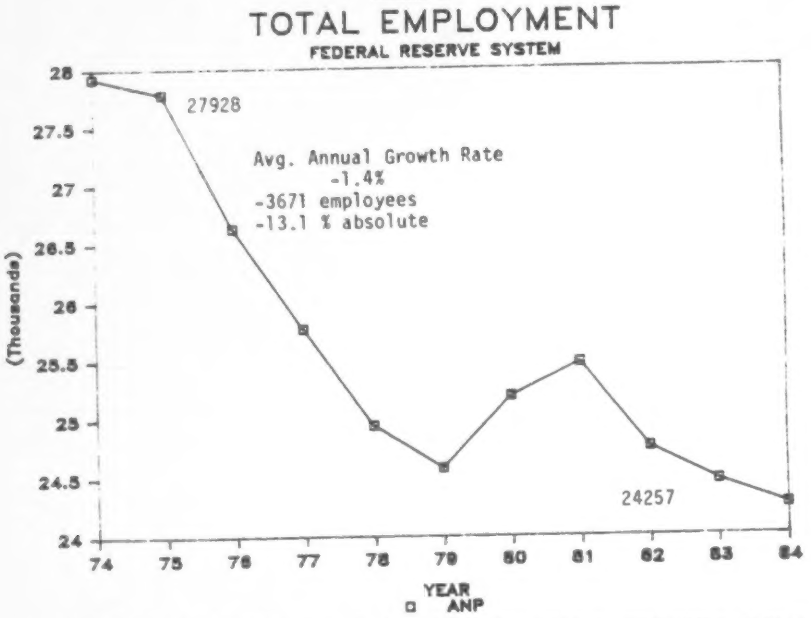


CHART 2



Note: These data include Reserve Bank and Board expenses, excluding currency costs, because the Fed reimburses the Bureau of Printing and Engraving for their total costs of producing Federal Reserve notes. Constant dollar data calculated using the GNP implicit price deflator 1972=100.

Table 1

Federal Reserve System
Expenditures, Employment and Volume Measures
1974-1984
% Change

	1974/1984	Average Annual Rate
Expenditures		
Real	7.2%	0.7%
Nominal	108.0%	-7.8%
Employment	-13.1%	-1.4%
Operating Volumes		
Funds Transfer	386%	17.1%
Currency	99%	7.1%
Check Collection	53%	4.3%

Table 2
Federal Reserve Expenditures
1984 Actual - 1985 Budget

	Federal Reserve System 1/ 1984 Actual - 1985 Budget (in millions)			Reserve Bank Expenses 2/ 1984 Actual - 1985 Budget (in millions)			Board of Governors Expenses 3/ 1984 Actual - 1985 Budget (in millions)		
	1984	1985	% change	1984	1985	% change	1984	1985	% change
Monetary & Economic Policy	130.2	131.7	1.1	99.4	98.4	- 1.0	30.8	33.3	8.1
Services to Treasury & Government Agencies	129.4	140.6	8.6	126.3	137.0	8.5	3.2	3.5	9.3
Services to Financial Institutions	728.2	757.9	4.1	701.5	730.3	4.1	26.7	27.6	3.3
Supervision and Regulation	158.1	174.4	10.3	140.7	156.7	11.4	17.4	17.7	1.7
Total	1145.7	1204.4	5.1	1067.8	1122.3	5.1	78.1	82.1	5.1

1/ These data are for Reserve Banks and Board of Governors expenses excluding currency costs. The data are derived from two separate accounting systems, for comparability over the time periods estimates were made to allocate expenses into major programs and for the Board of Governors which accounts for 7 percent of the total system expenditures.

2/ Includes support and overhead allocation.

3/ Includes depreciation expense. Figures may not add due to rounding.

Appendix A

HISTORICAL SUMMARY
FEDERAL RESERVE SYSTEM STRUCTURE AND BUDGETARY TREATMENT

Introduction

The budgetary independence of the Federal Reserve is part of a carefully constructed Congressional design to ensure the independence of the nation's monetary authority from day-to-day political influence. The Federal Reserve is not isolated from the Congress that created it: frequent testimony enables the Congress to oversee the Federal Reserve, to communicate its views, and to alter the Federal Reserve's operating functions, as it did in the Monetary Control Act of 1980, and in many previous legislative acts.

However, while the role of the Federal Reserve--and its budgetary independence--have been frequently reviewed both by the Congress and other groups, the conclusion has always been that it is in the nation's interest to retain the budgetary arrangements as the Congress originally framed them.

Background

The United States created its central bank much later in the nation's history than most other major industrial countries. The Federal Reserve System was established in 1913 following a string of bank failures and money panics. Six such economic crises had occurred in the preceding 30 years. With the most severe shock of 1907 still in mind, the 62nd Congress acted to create an institution that would preserve the value of U.S. currency and promote a stable economy.

The Federal Reserve Act, signed into law by President Woodrow Wilson on December 23, 1913, provided for:

> ...the establishment of Federal reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes.[1]

The Federal Reserve Act was crafted by Senator Carter Glass under the guidance of President Wilson. President Wilson made clear his desire for a decentralized central bank, composed of a system of regional reserve banks in which national banks, and voluntarily participating state banks, would be required to hold stock and maintain their reserves. He was equally adamant on the matter of dispersion of power and control stipulating that while six of each regional Reserve Bank's proposed nine directors would be chosen by banks, only three of these could themselves be bankers. The remaining three directors, including the Chairman, would be chosen by a separate Federal Reserve Board located in Washington and designed to be the capstone of the System.

The Federal Reserve's Budgetary Independence

Since the System's early years its independent status and its relationship to the Congress and the Executive have been the subjects of widespread discussion. The Congress carefully provided sufficient independence to enable the System to pursue the goal of maintaining a stable currency and economy insulated from day to day political influences and from the private banking community. The legislative history of the original Federal Reserve Act indicates that Congress was adamant on that point. Its exemption from the congressional appropriations process was seen as an essential part of this insulation, and the debate surrounding the passage of the Act is replete with statements reflecting this concern. The Federal Reserve Act specifically states that the Federal Reserve Board is to pay its expenses out of the earnings on Reserve Bank assets. It was clearly understood that the Reserve Banks themselves would not be subject to appropriations.[2]

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[1] Preamble to the Federal Reserve Act, December 23, 1913.

Major Legislation

- The Banking Act of 1933

The Congress passed the Banking Act of 1933 in an effort to strengthen the Federal Reserve Board and implement programs for economic recovery. It further clarified the Federal Reserve Board's and the Reserve Banks' independence by adding a new paragraph to section 10 of the Federal Reserve Act:

> ...The Board shall determine and prescribe the manner in which its obligation shall be incurred and its disbursements and expenses allowed and paid, and may leave on deposit in the Federal Reserve Banks the proceeds of assessments levied upon them to defray its estimated expenses and the salaries of its members and employees, ...; and funds derived from such assessments shall not be construed to be Government funds or appropriated moneys. (12 U.S.C. Section 244.)

According to both the House and Senate Banking Committee reports, the purpose of the amendment was to leave "to the Board the determination of its own internal management policies."[3] The Senate Report specifically states (pp. 11-12) that one of the purposes of the Act was to strengthen the Federal Reserve System by increasing the independence of the Federal Reserve Board.

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[2] See attached chronology relating to Federal Reserve legislative developments.

[3] S. Rep. No. 77, 73rd Cong., 1st Sess., p. 14, May 17, 1933.
H. Rep. No. 150, 73rd Cong., 1st Sess., p. 2, May 19, 1933.

o The Banking Act of 1935

The Banking Act of 1935 further strengthened the powers of the Board of Governors by removing the Secretary of the Treasury and the Comptroller of the Currency from the Board. A former Treasury Secretary, Senator Carter Glass, sponsored this amendment. He argued that the Secretary of the Treasury didn't belong on the Federal Reserve Board because of the chance that the Secretary would exercise undue influence on the Board, "treating the board as a mere bureau of the Treasury Department."[5] Glass said that Senator McAdoo, who had also been a Treasury Secretary, agreed with him. They believed that influence of this sort was not proper, and it was never contemplated that the Federal Reserve would function as an adjunct to the Treasury.

Although the American banking community lobbied for more control of the banking system when the Banking Bill of 1935 was being considered, they also expressed strong concern that the central bank not come directly under the influence of the Executive Branch. Political pressures would always be for inflation, they claimed, never for curbing the false prosperity of booms.

World War II and the Federal Reserve/Treasury Relationship

The Federal Reserve Board was given greater powers to control money and credit during World War II, but the Treasury's financing requirements necessarily dominated war time Federal Reserve policy. In an address in May 1948, Marriner Eccles said:

> The record of the financing of the war shows that as much as $8 billion a month was being spent, the public debt grew from around $40 billion to $280 billion in the short space of four or five years. The public debt was 60 percent of all debt. It would be perfectly obvious that in order to do that at a fixed interest basis, which was maintained throughout the war, we had to have a central open market operation. We were able to say to Treasury: 'We will finance whatever is necessary at the rates of interest now prevailing.' That was just before the war and we did.[6]

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[5] 79 Cong., Rec. 11,766-77 (1935).

[6] Address of Marriner S. Eccles, Chairman, Board of Governors of the Federal Reserve System to the Chairmen's Conference, White Sulfur Springs, West Virginia, May 29, 1948.

While this cooperative policy of war financing was obviously in the national interest, postwar support for government bond prices had long-term inflationary consequences, and the Board believed that supporting government bonds at a fixed rate was feeding inflation. In 1951 the Federal Reserve reached the historic "Accord" with the Treasury, which asserted the Fed's independence and relieved it of the responsibility of fixing the interest rate on Treasury debt issues.

Congressional Proposals

Putting the Federal Reserve System financing under the congressional appropriations process is not a new idea. Several proposals have been considered, but each time the Congress has decided to maintain the current system. The Congress has thereby succeeded in avoiding the problems that could arise if the nation's monetary policy were influenced by considerations of short-term expediency.

In 1964 the Congress held hearings entitled, "The Federal Reserve System After Fifty Years," in which a proposal calling for an audit by the GAO (H.R. 9631) was submitted, as was a bill (H.R. 9685) addressing the issue of putting the Fed under appropriations. Testifying on behalf of the Treasury before the House Committee on Banking and Currency, Secretary C. Douglas Dillon advised against taking such action:

> This committee is dealing with a living institution--an institution that has demonstrated its capacity to innovate, to experiment, and to adapt itself to a very wide range of circumstances. But in this process of change, it has never lost certain characteristics--an established tradition of independent judgment: a mixture of regional participation in policymaking with ultimate central control that is unique in our Government; an ability to attract highly qualified officials and staff; and a reputation for operating efficiently and impartially.

> Change without clear purpose can be dangerous too. If there are persuasive reasons for particular proposals--if it can be shown that ownership of Federal Reserve Bank stock by member banks has biased Federal Reserve policy decisions or if budgetary or auditing practices have been loose, to take two examples--by all means, this committee should act. But I doubt the advisability of taking action simply for the sake of achieving symmetry with other Government agencies particularly if there was danger that such action might impair a long tradition of regional participation and efficient service of which I believe the country can be proud.[7]

The legislation was not adopted.

In 1968, the House Banking and Currency Committee again held hearings on proposed structural changes to the Federal Reserve. The hearings on H.R. 11, chaired by Congressman Wright Patman, also addressed the issue of having the Congress appropriate operating funds for the Fed. In testimony the Treasury Department stated that subjecting the Fed to the appropriations process was unnecessary and "might widely be regarded as increasing the possibilities for reducing the independence of the System within the Government and as possibly leading to undesirable interferences with policies."

In 1975 the Senate Banking, Housing and Urban Affairs Committee considered a proposal to submit the Federal Reserve's budget to appropriations. Again, the argument was that such involvement by the Congress would largely dissolve the shield of relative independence from political influence that was built into the Federal Reserve Act. This principle was reiterated in a 1975 letter to Senator Proxmire from Joseph W. Barr, former Secretary of the Treasury, along with five other past secretaries, stressing how important they felt it was for the Federal Reserve to retain its status as a nonappropriated agency.

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[7] "The Federal Reserve System After Fifty Years," Hearings before the Subcommittee on Domestic Finance of the House Committee on Banking and Currency, 88th Cong. (Jan.-April, 1964.)

In 1978 with passage of the Federal Banking Agency Audit Act the Congress included an exemption from GAO audit for Federal Reserve transactions with foreign central banks and foreign governments, monetary policy matters, and any documents dealing with these topics. In passing this exemption, the Congress relied in large measure upon fears that information collected during the GAO audits (or GAO comments or criticisms) might be used to influence the System's policies for short-term political reasons. The key provision is the setting of limitations on the auditing process; one limitation is the absolute prohibition against auditing monetary policy matters.

Other Reviews of the Federal Reserve's Budgetary Status

In October 1967, the President's Commission on Budget Concepts presented its report, which led to the present federal unified budget concept. While the Commission found that the budget as a general rule should comprise the full range of federal activities, it did not recommend including the Federal Reserve in the budgetary process. The report observed that to do so might jeopardize the flexibility and independence of the central bank's monetary policy function.[8]

The Report of the President's Commission on Financial Structure and Regulation, also known as the Hunt Commission Report, stated in 1971 that "it is wise to keep the central bank and its decision making responsibility in a basically insulated position within the Federal Government." The Hunt Commission concluded that:

> The present position of the Federal Reserve provides for enough communication of ideas and coordination of action with the Executive Branch to serve the purposes of effective government. It also permits thorough and frequent review of central bank performance by the Congress to assure accountability to the public will. These vital safeguards are currently fully respected. The Commission strongly urges that the Federal Reserve System retain its present independence of decision-making to protect monetary policy from partisan political influences (Recommendation 13).[9]

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[8] Report of the President's Commission on Budget Concepts. (GPO, 1967) p. 28.

[9] The Report of the President's Commission on Financial Structure and Regulation, (GPO, 1971) p. 94.

More recently, in September 1976, in its report on the "Off-Budget Activities of the federal government," the House Committee on the Budget reviewed the budgetary status of a number of agencies exempt from inclusion in the budget. That report notes that the Board of Governors' budget (but not that of the Federal Reserve Banks) is included in the Appendix to the federal government's budget. Although the Committee recommended that a number of entities' budgets no longer be "off-budget," it chose not to review the expenses and budget status of the Federal Reserve.

Conclusion

The Federal Reserve's independence from the budget process has not isolated the Fed from the Congress. In 1978 the Congress passed the Full Employment and Balanced Growth Act, also known as the Humphrey Hawkins Act. It requires that the Board report twice a year to Congress on its monetary policy objectives and plans as they relate to the most recent Economic Report of the President. Rather than becoming involved in Federal Reserve System operations, the Congress has opted over the years to strengthen the System's reporting procedures and requirements. In the years since 1978, members of the Board or its staff have frequently testified before the Congress on many matters, including the Federal Reserve's budget.

The Federal Reserve System was created by the Congress in legislation carefully crafted to insulate the central bank from influences of private bankers, the Executive Branch and short-term political pressures in the Congress. This system has been examined and reexamined by committees of the Congress and independent commissions examining the banking and budget systems. All have concluded that the Congress acted wisely in establishing and maintaining the budgetary independence of the Federal Reserve System.

CHRONOLOGY OF MAJOR CONGRESSIONAL CONSIDERATION OF FEDERAL RESERVE STRUCTURE AND FINANCING

1913 Federal Reserve Act of 1913; Pub. L. 63-43: Determined structure of the Federal Reserve; designed as a regional system with a governing Board. Provided the Federal Reserve with unique status as an "independent" central bank within government, and organized its operation with the intent of insulating it from political pressures. The Act stipulated that the System's operating expenses were to be funded by assessments on earnings of the Reserve Banks. Ten percent of the Reserve Banks' net earnings was in a special surplus account maintained by the Treasury, and the remainder (90 percent) was paid to the U.S. government as a franchise tax.

1927 McFadden Act, also known as the Banking Act of 1927; Pub. L. 69-639: Extended the charters on the Reserve Banks for an indeterminate period (initially the Federal Reserve Act provided for renewable 20-year charters.) Certain restraints put on branch banking by state member banks in the FRS. American Bankers Association president testified that member banks want optional, rather than obligatory, contribution to capital of FRS and want "a voice in placing . . . reserve funds with approved Reserve agents as now, instead of all being impounded by law, and from the earnings of which the government abstracts a part." Because reserve funds are the property of the member banks, the member banks believed they should have a voice in how the funds are used. This view was not reflected in the act that passed. (House Banking and Currency Committee, Hearings on H.R. 6855, 68 Cong. 1 Sess. (GPO, 1924.))

1931-1932 Hearings on the Reconstruction Finance Corporation. The bill "requires the FR Banks to transact the business of this corporation, to receive deposits from it," but the Fed is not provided compensation for it, Glass said. During the hearings Glass contended that the Government owns not a dollar of interest in the Federal Reserve System. Undersecretary of the Treasury Ogden Mills says that the government has interest in the Federal Reserve System through the franchise tax. Glass questioned the arrangement saying the FR Banks were not government institutions. He said that the franchise tax (which has since been repealed) should not be collected any longer. He and Mills agreed that the FR Banks "do for government in its fiscal operations a tremendous amount of business without any compensation at all," and should be compensated. (H.R. 5060 and H.R. 5116, 72 Cong. 1 Sess., (GPO, 1932.))

1932-33 Hearings on Operation of the National and Federal Reserve Banking System in the U.S. Senate (later became the Banking Act of 1933). In discussion before the Senate Banking Committee, Eugene Meyer, Chairman of the Board, and Senator Glass discussed government financing of emergency recovery programs and institutions. Meyer said that the government had not contributed any money to the maintenance of the Federal Reserve System, and Glass said that it never should. Glass reiterated: "The government does not own one dollar of proprietary interest in the Federal Reserve System, and I for one have been intent on keeping it that way. I don't think the government should have anything to do with it except by way of supervisory control." (S. Res. 71, 71 Cong. 3 Sess. (GPO, 1932.))

1933 Banking Act of (June 16) 1933, Pub. L. 73-66: In addition to important changes in operating procedures and structure of FOMC, the Act stated that funds of the Federal Reserve System, the FDIC and the Comptroller of the Currency were not public moneys. Subsequently the Federal Reserve was not subject to GAO audit, or the appropriations process. Federal Reserve surplus account funds used to capitalize the FDIC. Franchise tax requirement was eliminated to enable the Reserve Banks to restore their surplus accounts. To strengthen the Board's political independence, terms of governors were extended from 10 to 12 years. (S. Rep. 77, 73 Cong. 1 Sess., (GPO, 1933.))

1934 Hearings of the House Appropriations Committee on H.R. 9410; Permanent Appropriations Repeal Act, 1934. All government agencies were required to address Congress on their budgetary status. Testimony given regarding the Federal Reserve's special status. These hearings constituted the only written explanation (as far as can be determined) of the amendment. Testimony explicitly addressed the language in the 1933 Banking Act formally granting the Federal Reserve its financial independence. Testifying on behalf of the Board was Chester Morrill, Secretary of the Board and chief administrative officer. He was, in part, responsible, along with Senator Carter Glass, for the provision in the 1933 Banking Act that the Federal Reserve's funds were "not to be construed as government funds or appropriated moneys." Morrill said that the Federal Reserve had never considered the funds to be anything else.

"We do not agree that they were ever public moneys or appropriated moneys." Nothing was ever done about it until ... the Banking Act of 1933 when Senator Glass "who took very great exception" to that idea, "objected to any such idea being permitted to exist, and incorporated into the Banking Act an amendment to the Federal Reserve Act to that effect." (H.R. 9410, 73 Cong. 2 Sess., (GPO, 1934.))

1935 Banking Act of 1935; Pub. L. 74-305: The FOMC was created in its present form; salaries of Board members were improved to help attract qualified individuals and to restore to the Board the stature to which it was legislatively entitled. Independence was further defined and promoted by extending terms of governors from 12 to 14 years and removing the Secretary of the Treasury and Comptroller of the Currency from the Board.[1]

1938 Hearings on "Government Ownership of the Twelve Federal Reserve Banks," H.R. 7230, sponsored by Wright Patman, before the House Banking and Currency Committee, chaired by Congressman Steagall. Instead of concentrating on whether the Federal Reserve Banks "shall be the property of the United States;" the hearings were used by the Housing Banking Committee to question Federal Reserve officials, such as Chairman Marriner Eccles, on monetary policy and System operations. (H.R. 7230, 75 Cong. 3 Sess. (GPO, 1938.))

The bill also recommended expanding the Federal Reserve Board to 15 members, including the Treasury Secretary, the Comptroller of the Currency, and Chairman of the FDIC. The bill was not seriously considered.

1945 Senate hearings on the "Government Corporation Control Act" on providing for financial control of Government Corporations. The General Accounting Office expressed the view that the Reserve Banks should be excluded from the Act because they were examined frequently and thoroughly by examiners under the direction of the Board of Governors. (Expenditures in the Executive Department's Committee Hearings on H.R. 2177, 79 Cong. 1 Sess., (GPO, 1945.))

1949-1950 Douglas Committee. Report of the Joint Economic Committee issued. Key recommendations stated that credit policies must be flexible and the Federal Reserve System must remain independent of executive domination. Hearings before the subcommittee on monetary, credit and fiscal policies (81 Cong. 1 Sess., pursuant to Sec. 5A of Pub. No. 304 (GPO, 1949.))

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[1] Before enactment of the 1935 Banking Act, the title "governor" referred to the chief executive officer of the Board, and there were eight Board "members" on the Board. With passage of that Act their titles were changed to governor. As a result, the Board had seven governors and a chairman.

1952 Patman hearings on General Credit Control and Debt Management before the Joint Economic Committee. Overwhelming weight of testimony favored independence of the Federal Reserve from political pressures and agreed on the inherent inflationary risks in using the Federal Reserve to supply the Treasury with cheap credit. Congressman Patman indicated that his interest in government audit of the Federal Reserve was not only for information, he wanted Congress to exercise control over income and expenditures by the Board and the Reserve Banks so that it could influence the policies of the System. "I do not mean inconvenience just to inconvenience you (the Fed) but I mean quickly to pass upon policies."

No mandate issued from Congress but the Federal Reserve furnished its own audit reports to appropriate congressional committees for inspection. (Subcommittee on General Credit Control and Debt Management, 82 Cong. 1 Sess., (GPO, 1951-1952.))

1964 Hearings on "The Federal Reserve System After Fifty Years": Proposals made for improvement of Federal Reserve and introduction of H.R. 9631 calling for audit by the GAO; and H.R. 9685 addressing the issue of the Federal Reserve being put under appropriations by Congress. After the conclusion of these exhaustive hearings, Congressman Hayes summed up the committee's overall evaluation: "If there were any evidence of corruption or bad management, inefficiency, I think there would be a prima facie case for making some change. But it seems to me that the reputation of the Federal Reserve System for integrity and honesty in the way they handle their affairs is unrivaled." (Proposals for the Improvement of the Federal Reserve, and Staff Report, Subcommittee on Domestic Finance of the House Committee on Banking and Currency, 88 Cong. 2 Sess. (GPO, Aug. 1964.))

1968 The House Banking and Currency Committee Report on H.R. 11, proposed by Congressman Wright Patman. Proposed structural changes to the Federal Reserve System, among them: an annual audit of the Board and Reserve Banks and Branches by the Comptroller General of the U.S. and operating funds for the Federal Reserve System to be appropriated by Congress. The Treasury Department stated that the measures (either government auditing or subjecting the Fed to appropriations process) were unnecessary and "might widely be regarded as increasing the possibilities for reducing the independence of the System within the Government and as possibly leading to undesirable interferences with policies." The hearings did not result in legislation.

The Treasury further noted that Congress has also exempted other major bank supervisory authorities--the FDIC and the Comptroller of the Currency--from the regular appropriations process. (Compendium on Monetary Policy Guidelines and Federal Reserve Structure pursuant to H.R. 11, 90 Cong. 2 Sess. (GPO, December 1968.))

1975 The Senate Banking, Housing, and Urban Affairs Committee hearings on S. 2285 and S. 2509 chaired by Senator William Proxmire. Consideration was given to a proposal to limit expenditures by the Board of Governors and the Federal Reserve Banks to amounts approved in appropriations acts. (Hearings before the Senate Banking, Housing and Urban Affairs Committee on S. 2285 and S. 2509, 94 Cong. 1 Sess. (GPO, 1976.)) Similar hearings held 1977-1980 by Senate banking Committee covered substantive issues as well as budgetary issues.

1977 Federal Reserve Reform Act of 1978, Pub. L. 95-188: Amendments passed that provided for Senate confirmation of Board's Chairman and Vice Chairman and for the extension of conflict of interest provisions to Federal Reserve Bank directors, officers and employees. This action was seen by Congress as a way of making Federal Reserve management more accountable to Congress.

1978 Federal Banking Agency Audit Act of 1978; Pub. L. 95-320: Congress authorized the GAO to perform audits of banking agencies but included an exemption from GAO audit for Federal Reserve transactions with foreign central banks and foreign governments for monetary policy matters and for any documents dealing with these topics. In passing this exemption, Congress relied in large measure upon concerns that information collected during the GAO audits (or GAO comments or criticisms) might be used to influence the System's policies for short-term political reasons. Full Employment and Balanced Growth Act; also known as the Humphrey-Hawkins Act; Pub. L. 95-523: Requires that the Board report twice a year to the House and Senate Banking Committees on its monetary policy objectives and plans as they relate to the most recent Economic Report of the President. (Hearings before the Senate Governmental Affairs Committee on H.R. 2176, 95 Cong. 1 Sess. (GPO, 1978.))

1980 Monetary Control Act of 1980; Pub. L. 96-221: Required that all depository institutions be subject to reserve requirements set by the Board. Also required the Federal Reserve Banks to charge depository institutions for services.

The GAO report entitled "Response to Questions Bearing on the Feasibility of Closing the Federal Reserve Banks" concluded that there were no overbearing reasons for closing the Federal Reserve Banks. The study also stated that "no alternative to the banks presently exists." House Banking, Finance and Urban Affairs Committee, Hearings on H.R. 7; 96 Cong. 1 Sess. (GPO, 1979.))

1985 The Congressional Budget Office Report on "The Budgetary Status of the Federal Reserve System:" CBO addressed three budgetary options for Congressional treatment of the Federal Reserve. In testifying before the JEC on the results of the study, the director of the Congressional Budget Office noted that the risks of reducing the Federal Reserve's independence on policy matters is greatest if Federal Reserve expenses are appropriated and if the Reserve System is required to project its financial operations. The risk is smaller (but still exists) if the budgetary coverage is primarily informational and limited to operating expenses.

Appendix B

FINANCIAL INDEPENDENCE OF CENTRAL BANKS OF THE G-10 COUNTRIES[1]

While detailed arrangements differ from country to country, in general the central banks in the G-10 countries have a high degree of budgetary autonomy, even in countries where the central bank has less autonomy than the Federal Reserve in determining monetary policy. Budgets are developed and implemented by the central banks themselves. The degree of subsequent central government review varies from modest to none (except in Japan where a more extensive review takes place). In no case is the central bank's budget submitted to the legislature or parliament for formal review or included in the central government's budget.

The degree of independence of G-10 central banks is summarized in Table A. Following is a more detailed description of each of the G-10 central banks with regard to budget processes and earnings distributions.

BELGIUM

1. Budget process. The National Bank of Belgium drafts its own budget. A government official then reviews the budget to see if it is in accordance with the general thrust of government budgetary policy. The Bank, as a rule, tries to stay within the overall guidelines of the government, but it is not legally obligated to do so and the process of reconciling views of the Bank and the government on budgetary matters is informal.

2. Earnings distributions. The amount of profits that the Bank returns to the government is determined in part by formulas described by law and in part reflects discussions between the Bank and the Ministry of Finance. In recent years only about 7 percent of net profits have been added to reserves with the remainder going to the government.

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[1] The G-10 countries now include Switzerland.

CANADA

1. Budget process. The Bank of Canada's yearly budget is drawn up by the Bank's staff under the direction of the Governor of the Bank and submitted for approval to the Bank's Board of Directors. (The Board consists of five directors, including the Deputy Minister of Finance serving *ex officio*.) The Bank's functions as the government's fiscal agent (primarily involving debt management and foreign exchange transactions) are audited by the Auditor General. The Bank's own affairs are audited by two external auditors appointed by the cabinet on the recommendation of the Minister of Finance.

2. Earnings distribution. The central government has received all profits of the central bank in recent years. At times in the past, the Bank of Canada used a portion of its profits to build up an internal contingency fund. However, the relatively low statutory ceiling on the size of this fund was reached a number of years ago, and since then all profits have gone to the government.

FRANCE

1. Budget process. The Bank of France has the authority to set its own budget. Normally, however, the Bank voluntarily follows any government policies setting limits on overall spending increases in government agencies. The Bank pays for its budgetary expenses out of income earned from its operations.

2. Earnings distribution. All profits are turned over to the Treasury.

GERMANY

1. Budget process. The Bundesbank's budget is set by the Central Bank Council. This procedure is not a part of the overall government budget process. In accordance with German corporate law, the Bank publishes an annual income statement.

2. Earnings distribution. Almost all Bundesbank profits have recently been distributed to the central government. In the past, significant additions to reserves have also been made. The law governing the Bundesbank provides that up to 20 percent of annual profits should be added to a reserve pool, so long as cumulative contributions do not exceed an upper limit of 5 percent of the notes and coins in circulation. A further 10 percent of annual profits can be added to reserves within certain restrictions. Recently, only small additions to reserves have been made, with nearly all profits (98 percent in 1984, the most recent year for which data are available) distributed to the central government.

ITALY

1. Budget process. The Bank of Italy is autonomous in regard to budget and salary matters. The Bank submits its budget once a year for ratification by the Treasury, which is generally pro forma.

2. Earnings distribution. Over half of the Bank's profits are turned over to the Treasury, with the remainder going into a reserve account.

JAPAN

1. Budget process. The budget of the Bank of Japan is not included in the central government's annual budget. However, the Bank's budget must be submitted to, and approved by, the Ministry of Finance, which has occasionally required the Bank to alter proposed budgets. The Bank's budget and expenditure practices are also subject to examination by the Board of Audit, a separate government agency roughly akin to the U.S. General Accounting Office.

JAPAN, cont.

2. Earnings distribution. All profits are turned over to the government.

THE NETHERLANDS

1. Budget process. The Netherlands National Bank sets its own budget and is not subject to budgetary control by the central government.

2. Earnings distribution. Earnings from the Bank's operations over and above its expenses are generally turned over to the Treasury.

SWEDEN

1. Budget process. The areas in which the Swedish Riksbank may make expenditures are limited by law, but the government does not set the Riksbank's budget. Indeed the Riksbank does not appear to have a formal budget, although it does maintain personnel, administrative, and some other budgets as forms of internal control.

2. Earnings distribution. The Riksbank determines the amount of profits to be returned to the Treasury. A large proportion of earnings is simply put into reserves.

SWITZERLAND

1. Budget process. The Swiss National Bank is essentially autonomous in its budget-making authority. The budget for the Bank's operation does not need the approval of government ministers or the Federal Council. The Bank's Annual Report, which details its expenditures, earnings and reserve accumulations, is submitted to the Federal Council.

2. Earnings distribution. In Switzerland, the central bank is a private corporation. As part of its expenses the central bank pays a (small) fixed dividend to shareholders, makes a stipulated (small) addition to reserves, pays federal income tax to the central government, and makes a fixed per capita distribution to the local cantons. The law provides for distribution, two-thirds to the cantons and one-third to the federal government, of any net profits resulting from earnings above expenses and after additions to reserves. In practice, the Bank has chosen to exercise its rights as a private corporation and has added to its reserves each year in amounts large enough to leave no net profits after additions to reserves. As a consequence, the federal government has received almost none of the Bank's earnings.

UNITED KINGDOM

1. Budget process. The Bank of England has a high degree of autonomy in determining its own budget. The Bank draws up its own annual operating budget which must be approved by its Court of Directors. While the government never directly reviews the Bank's budget, it can have an indirect influence on the Bank's expenditures. About half the Bank's income is from fees the government pays for services the Bank performs, mainly marketing government debt and acting as the government's fiscal agent. The fees which the Bank charges the government for these services are reviewed annually, giving the government an opportunity to raise questions about the costs of the Bank's operations on its behalf.

2. Earnings distribution. The profits of the Bank of England are derived from the Issue Department (concerned with the provision of currency) and the Banking Department (dealing with all other central bank matters). All profits of the Issue Department are turned over to the Treasury. Profits of the Banking Department are divided into three different parts. One part, consisting of a payment in lieu of dividends as spelled out in the Bank of England Act, goes to the Treasury. Another part goes to the government in the form of corporate taxes. The remainder is transferred to reserves. Since profits of the Issue Department have been much larger than profits of the Banking Department, only a small portion (about 2 percent in recent years) of total profits have been added to reserves, with the rest (about 98 percent) distributed to the Treasury.

Conclusion

In all of the G-10 countries, budgets of the central banks are handled outside of the normal governmental appropriations process. Each of the central banks finances its expenditures out of its own income (mainly interest earnings on their portfolio holdings). Profits in excess of expenses are then turned over to the government or added to reserves in varying degree. In no case is a budget statement for the central bank listing the bank's expenses and receipts included in the central government's budget document. In all cases except Switzerland (where no central bank profits have been turned over to the central government in recent years), the central government's budget does contain a line for profits received from the central bank.

Table A

The Budgetary Independence of Central Banks of G-10 Countries[2]

	Is the central bank subject to the normal governmental appropriations process?	What is the degree of the government's review of the central bank's own budget proposals?	What percentage of the central bank's profits after expenses has been turned over to the government in recent years?
Belgium	No	Low	95%
Canada	No	Low	100%
France	No	Low	100%
Germany	No	None	95%
Italy	No	Low	50%
Japan	No	Moderate	100%
The Netherlands	No	None	100%
Sweden	No	None	60%
Switzerland	No	None	0%
United Kingdom	No	Low	95%

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[2] The G-10 countries now include Switzerland.

Appendix C

PLANNING, BUDGET AND CONTROL PROCESSES OF THE FEDERAL RESERVE SYSTEM

Both the Reserve Banks and the Board of Governors use an annual, calendar year planning, budget and control process. Each process has been developed to ensure that objectives and goals are met in an efficient and effective manner. Following is a detailed description.

I. RESERVE BANKS

The planning process for the Federal Reserve Banks includes strategic planning and short-term tactical planning at the System and Reserve Bank levels. Major goals, objectives and strategies are identified during the planning process. The budget process includes the identification, review and approval of resources needed to achieve goals and objectives. The control process includes the comparison of actual results against planned goals and objectives, and the comparison of actual financial performance against the approved budget.

The Planning and Control System (PACS)

In 1977, the Federal Reserve Banks implemented a new accounting and budgeting system, PACS, which allows for a more effective review of expenses, an expense audit trail and an expense accountability structure. PACS is a uniform expense accounting, cost accounting and reporting system that enables the Board to compare Reserve Banks' financial performance and facilitates uniform expense aggregation among Reserve Banks and Branches. The PACS system also serves the control function by allowing for comparisons of actual performance against budget at a detailed object and activity level.

A uniform chart of accounts and functional grouping of expenses are identified in PACS. Costs are identified at a detailed expense level--such as officer salaries--and are separated into three groups: direct, support and overhead. All costs are accumulated by major function, the largest aggregation being the four primary missions of the Federal Reserve System: (1) Monetary and Economic Policy; (2) Services to the U.S. Treasury and Other Government Agencies; (3) Supervision and Regulation of Financial Institutions; and (4) Services to Financial Institutions and the Public. All support and overhead costs are fully redistributed or allocated to these four major service lines.

PACS provides productivity statistics (primarily unit cost and items per manhour), environmental statistics (to clarify the differences between Banks' operating environments) and quality statistics. PACS also allows for separate accounting and reporting of project costs that are not involved in routine production of activities and services.

The PACS system was designed prior to passage of the Monetary Control Act which required pricing of the Federal Reserve's payment services. Since then, PACS has been modified to reflect the need for different and changed information regarding priced services. It continues to serve as the fundamental accounting system for all services the Federal Reserve Banks provide, priced and nonpriced.

Over time, the PACS process has been studied by government agencies, private organizations, the General Accounting Office and outside public accounting firms. The PACS system has been judged to be very effective and several agencies have studied its design for their own use.

The Board periodically audits Reserve Bank compliance with the PACS instructions through on-site operations reviews. These audits have affirmed Reserve Bank compliance with the PACS instruction. Similarly, independent examinations have determined that PACS is an appropriate and effective accounting mechanism for the Federal Reserve.[1]

Impact of Pricing on Process

The Monetary Control Act of 1980 (MCA) had a much larger impact on the System's planning, budgeting and control process than just its impact on the PACS system. Before pricing, the sole objective of the budget process was to control resources and minimize the growth of expense. Reserve Banks were encouraged to compete against each other to realize the lowest expense and greatest productivity increases.

With the MCA, the process had to be adjusted to include other objectives such as the legislated mandate of full cost recovery for priced services Beginning in 1983, the planning, budget and control process was divided into two primary areas for compilation, reporting and analysis purposes--Central Bank and Treasury Services and Priced Financial Services.

Essentially, the more traditional approach used in Federal Reserve budgeting continues to be applied to services in the Central Bank and Treasury Services sector; the emphasis remains on holding down expense growth and cost minimization. District trends are carefully compared to System trends. For priced services, an approach more akin to that employed by private business is utilized--with emphasis on recovery of costs and achievement of business objectives. The planning process now includes business planning for priced services, and necessarily, the control process includes monitoring Reserve Banks' cost recovery performance for priced services.

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[1] Comptroller General of the United States, Report to the Chairman, Committee on Banking, Housing and Urban Affairs, United States Senate, "An Examination of Concerns Expressed about the Federal Reserve's Pricing of Check Clearing Activities." January 14, 1985.
Arthur Andersen & Co., "Federal Reserve System: Report on Priced Services Activities." Forthcoming, 1985.

In addition, the MCA has resulted in changes to the System's management process. Reserve Banks are now required to have their financial plans and prices for their priced services reviewed by Product Directors and a Pricing Policy Committee as well as the Board of Governors.

The Budget Schedule

At the beginning of each calendar year, the budget planning process begins with the development and approval of budget guidelines based on an assessment of workload and productivity changes forecasted for the budget year. The annual budget objective includes these guidelines and is used by the Reserve banks in the development of plans and budgets. In addition, a strategic directional statement covering three years is developed to guide the Reserve Banks in the development of priced service business and financial plans. In the spring, the Reserve Banks develop their own goals, objectives and strategies and begin their budget process. During the summer the budgets are reviewed at the Reserve Banks, and in the fall the Board of Governors reviews and approves the Reserve Bank budgets.

The Reserve Banks' Planning Process

System Level

Senior management officials of the Reserve Banks and Board staff discuss significant issues in the course of meetings throughout the year. These discussions focus management attention on key issues and the need to make effective use of resources to meet agreed upon objectives. The annual Reserve Banks' Budget Objective and the strategic guidelines for priced services are additional elements for planning at the System level.

Reserve Bank Level

Planning occurs at each Reserve Bank as well as at the System level. Although the services provided by each Reserve Bank are similar, the conditions confronting the Reserve Banks differ markedly. Some are located in areas in which unit banking predominates; others serve large branch banking organizations. Rates of regional economic growth differ markedly among the Reserve Banks, as do wage levels, labor skills and prices of other inputs. The importance of these differences in environmental conditions has increased with the advent of pricing. Effective resource control thus makes it essential for individual Reserve Banks to engage in detailed planning.

The Budget Process

For nonpriced services, the Board of Governors each year formally approves a budget expense limit in the form of a percentage increase over the expense level in the current year. The process begins early in the calendar year when an advisory group is formed under the Conference of First Vice Presidents to make recommendations to the Conference (and ultimately to the Board of Governors) on basic budget assumptions for the upcoming year. The Budget Objective Advisory Group makes economic assumptions for the budget year, and assesses major legislation and other factors influencing the System's responsibilities. An aggregate expense guideline is established for the total of all Central Bank and Treasury (nonpriced) Services; and the cost recovery objective for priced services is reaffirmed. The Advisory Group's recommendation is forwarded to the Conference of Presidents and the Conference of First Vice Presidents prior to submission to the Board.

At the Board, a thorough review is conducted of the assumptions made and a budget objective is approved by the Board of Governors in an open Board meeting. The budget objective is then sent to the Reserve Banks and serves as the overall top management guide for formulating Reserve Bank budgets. The budget objective serves as a challenging goal for the Reserve Banks and helps ensure that financial planning among the Reserve Banks is consistent. During the Board's subsequent review and approval of Reserve Banks' budgets, compliance with the Budget Objective is carefully considered.

An example of the process used by a Reserve Bank follows:

At the onset of the budget cycle, a Reserve Bank initiates planning efforts to direct upcoming events. Senior management (President, First Vice President, and other senior level officers) identifies and/or modifies the broad strategic direction for the next few years. Senior management also establishes for Bank operations a District Budget Objective for central bank and Treasury services (nonpriced areas) that reflects the System Objective as well as any other factors unique to the Reserve Banks. For priced services, the primary objective is to match costs with revenues. The strategic direction, coupled with the Bank's own Budget Objective, sets the stage for the budget process.

Based on the strategic direction, middle management develops more detailed plans for each of its functions. The budget numbers are then based on these detailed plans.

For expense budgets, management of each department is asked to budget for nearly all expenses. Wherever possible, departments are expected to zero-base the estimates, especially for expenditures such as travel, training and education, etc. In those instances where technical expertise is required the budget estimates are developed centrally for the entire Bank. For example, the budget estimates for automation expense are developed by staff experts familiar with the Bank's systems and with anticipated changes in the industry. The total estimate is then apportioned to departments based on anticipated usage. In some cases, departments use a uniform budget assumption provided by a central area to ensure bank-wide consistency, e.g., a department applies a factor for an expected office supply cost increase (developed by the purchasing function) to its usage-based estimate.

Because salary and benefit expense accounts for a large part of a Bank's expense budget (about 60 percent), Bank management closely scrutinizes the salary plans. Each Division's management estimates its staffing needs for the remainder of the current year and for the upcoming calendar year. Senior management reviews proposed staffing changes, which are sometimes reduced as a result. To achieve consistency, the personnel function develops the Bank's estimates related to administration of the salary program for merit and other salary increases. The Fed does not have any automatic cost of living increases. The analysis includes a projection of the effect of turnover rates and lags in filling open positions. Much attention is also devoted to evaluating the predicted salary movements in other local corporations as well as the salary conditions and guidelines set forth in the System Budget Objective. The overall Bank projection is closely reviewed by the First Vice President and, upon approval, applied to each department's budget.

Department management is responsible for reviewing its budget increase against the Bank's objective and for justifying any exceptions to the guideline. Finally, a central budget analysis function compiles all the budget data, makes comparisons with historical trends and notes any questionable areas requiring senior management's attention. The budget staff often presents budget alternatives for senior management's review. A summary of all budget data by major responsibility is then presented to the First Vice President for review. Each division head and branch manager must present his/her budget, staff projections, and supporting rationale to the First Vice President. As a result of this close scrutiny, adjustments to the budget data are sometimes required.

Once the necessary adjustments are completed, an executive summary of the overall budget is prepared and forwarded to the Bank's President and First Vice President. Following their approval, the budget package is sent to an Executive Committee of the Board of Directors. After the Committee's review, the budget is presented for approval to the Board of Directors with the Executive Committee's recommendation for action. The final step is to secure approval from the Board of Governors.

During the budget year, senior management closely reviews actual performance against the budget on a monthly basis. Depending on the results of these monitoring efforts, it is sometimes necessary to adjust spending plans for the rest of the year.

System Projects

Certain Reserve Bank expenditures are associated with major research and development projects undertaken for the benefit of the entire System; therefore, all Districts must bear a share of the costs incurred. Budgets must be prepared and approved for these shared costs so that each Reserve Bank can include its portion of the shared cost in its annual budget.

Budgets for such projects are reviewed by the sponsoring Conference of First Vice Presidents' Subcommittee/Committee, Board staff and other responsible System groups. After these reviews are completed, the budgets are approved by the Conference of First Vice Presidents and the allocated costs forwarded to the individual Reserve Banks for inclusion in their respective budgets. This process occurs between March and July of each year and affords an extra level of scrutiny on significant projects underway in the System.

Capital Budget Process

The Reserve Banks' planning, budgeting and control process includes the preparation, review and approval of capital outlay schedules. Reserve Banks annually evaluate needs for building, furniture, furnishing and fixtures, land and automation equipment. In accordance with generally accepted accounting principles (GAAP), depreciation of capital assets is included in Reserve Banks' expenses. All large capital expenditures undergo a thorough review separate from the actual planning, budgeting and control process. Acquisitions of mainframe computers and peripheral equipment, at certain dollar levels, must be approved by the Board of Governors on a case by case basis.

The Board has established detailed, comprehensive guidelines for preparation of Reserve Banks' proposals for the purchase of capital assets. In a new building program, these guidelines are exhaustive and compose more than 70 pages in a Facilities Planning Manual. The Board must approve the project at various stages of construction. The Automation Procurement Guidelines cover the procedures for justifying acquisitions in this category.

Expert technical staff at the Board review all proposals and make recommendations to the Director of the Division of Federal Reserve Bank Operations or to the Board of Governors, depending on the approval level. The Board considers these procedures extremely effective in controlling Reserve Banks' expenses.

Federal Reserve Banks' Budget Review at the Board of Governors

Reserve Bank budgets are forwarded to the Board in the fall. Budget analysts at the Board review the budgets and note significant Systemwide issues which need to be addressed during the budget review. Reserve Bank budget data are received at the Board via automated transmission and are thus easily aggregated and subjected to analysis. The narrative justifications of the budget data, particularly the executive summaries and the statements of objectives, are analyzed in terms of the Bank's own trend in past years, the level of increase in specific areas compared to that of other Districts, and in terms of compliance with the System Budget Objective and cost recovery objectives for priced services.

Budget data consist of the major expense objects which comprise the total budget such as salaries, equipment, supplies, etc., the major service lines and services, as well as revenue and volume estimates. From each Reserve District information on about 19 expense objects and 49 services are received and reviewed at the Board. Employment data for the 49 services are also received and analyzed as are data on the following:

a) system projects
b) salary expense components
c) benefits
d) selected volume and unit cost estimates
e) capital outlays (by eight classes)
f) costs and revenues by priced services
g) priced volume projections

In conjunction with the budget analysts, personnel in the Division of Federal Reserve Bank Operations who are expert in particular services performed at Reserve Banks review each Reserve Bank's budget as it relates to their area of expertise. These persons identify questions regarding budget objectives and initiatives and evaluate the resource requirements budgeted in light of their special knowledge of services and problem situations at particular Banks.

In addition, staff of the Board's Personnel Division carefully review sections of the budget related to salaries and benefits. This staff is also responsible for the review of salary and benefit administration at the Reserve

Banks throughout the year and are knowledgeable about local business environments. Budget proposals are reviewed relative to local labor market data, known problem areas and specific administration considerations.

Also, the Product Directors, the Pricing Policy Committee and the Board review Reserve Bank priced service budgets and process proposed for the budget year. This combined review successfully accomplishes the integration of price and budget review into one overall review of Bank objectives. The various reviews yield issues and questions to be explored at the budget meetings held in the fall with the Reserve Bank Presidents and the Committee on Federal Reserve Bank Activities (consisting of three Governors).

The budget analyst assigned to the particular Reserve Bank assembles all issues and questions raised during the review phase. These questions, which may be as high as 50 in number, are wired to the Reserve Banks and written explanations are received and analyzed to determine if further review is necessary.

The most important issues become the agenda for the Reserve Bank's budget meeting, which is scheduled with each Reserve Bank President and the Committee on Federal Reserve Bank Activities whose function it is to critique the Reserve Bank budget being proposed. The staff briefs Committee members on the important issues and problems to be discussed with the Reserve Bank President. Board staff will often make recommendations to the Committee regarding actions the Reserve Bank President should be asked to take before final budget approval by the Board of Governors.

At the budget meeting, the First Vice President and the Reserve Bank's Senior Financial Officer usually assist the Reserve Bank President. Although there is no set format for each meeting, each party usually has time to make a summary statement before specific issues, problems, and questions are addressed. Fundamentally, the budget meeting serves as the occasion when the top management of the Reserve Banks and the Board of Governors reach consensus on that particular Reserve Bank's plans and budget for the coming year. After the 12 District budget meetings, the Reserve Banks make whatever changes the Committee requires and a new iteration or final District budget is determined. Board staff receives the final budget and reviews it for compliance with the agreements reached during the budget meeting.

Budget Approval

When the Committee on Federal Reserve Bank Activities is satisfied with each Reserve Bank's budget, these budgets are sent to the Board of Governors for approval. Budgets are reviewed and approved at an open meeting of the Board of Governors. Subsequently, a letter is sent to each Reserve Bank President stating the budget level approved by the Board and any budget conditions placed on this budget level.

The Monitoring and Control Process

District expenses are monitored and controlled at both the Reserve Banks and the Board of Governors. The Reserve Banks are permitted flexibility to move approved levels of spending within expense and services structure; however, the Board guidelines require notification on significant reallocations of approved budget levels. Careful monitoring minimizes overruns and increases flexibility by permitting transfers.

Nonpriced Services

Because the Reserve Banks budget and report expense in the same cost components (PACS), a comparison of budget to actual spending is possible at the lowest level of budget detail. Expenses are reported on a quarterly basis to the Board, and, as soon as possible following receipt of actual data, a comparison of actual expense to budgeted expense is made.

Priced Services

The establishment of prices for Federal Reserve services mandated by the MCA has resulted in additional review of Reserve Bank expenses. Detailed product level information is needed as well as timely monitoring of performance. A cost/revenue/volume reporting process collects and records financial data relative to priced services. The establishment and approval of prices and the effective monitoring of priced services performance are key elements in the overall management of Reserve Bank resources. However, market discipline is the focal point when costs of Federal Reserve priced services are considered. Full costs must be recovered in the marketplace or the service must be eliminated. This discipline helps guarantee that costs in the priced services areas are no greater than necessary.

Board staff also prepares an annual report to the Board of Governors on Reserve Bank budget, employment, unit cost and volume performance. As needed, a detailed mid-year review is sometimes conducted to ensure that budget levels are being achieved.

II. BOARD OF GOVERNORS

The Board has an annual planning, budget and control process that involves all Divisions at the Board and all management levels. The Chairman has appointed the Administrative Governor to assume oversight responsibility of Board administrative and management matters. The Administrative Governor has a key role in the entire Board process in ensuring that all elements of the process are coordinated, that responsibility for all objectives is complete, that resources are adequately provided, and that duplication of effort is avoided.

In addition, activities of each Division and Office are divided into groups called Programs. These Programs are the level at which resource planning is conducted, plans are approved and budgets are prepared.

The Board's Program Structure

The Board of Governors has adopted a Program Structure which reflects Board resources by categories along functional lines consistent with System responsibilities. Both expenses and employment are organized into four major areas: (1) Formulation of Monetary Policy; (2) Supervision and Regulation of Financial Institutions; (3) Financial Services to the System, the Government, and the Public; and (4) System Policy Direction and Board Support. Data processing costs are distributed to the four major areas based on usage. Other support and overhead responsibilities are included in category four.

The Budget Schedule

The Board of Governors budgets on an annual calendar year basis. At the beginning of the year, the staff seek guidance from the System's strategic planning sessions and from legislative and economic developments and use this information to develop budget guidelines. In the spring, a budget target is established to guide budget development. The Divisions prepare their budget, including program objectives and expense and employment requests, during the summer. In the fall, the Division budgets are submitted to the Office of the Controller, which along with the Staff Director for Management, reviews each budget. In addition, the Board Oversight Committees review their respective Division budgets. And finally, the Administrative Governor reviews the budget and forwards it to the Board of Governors for approval in December prior to the beginning of the calendar year.

The Budget Process

The budget process at the Board of Governors begins with the establishment of a budget expense limit in the form of a percentage increase over the current year's estimated expenditure.

In early spring each Division is requested to review current and future resource needs. Each Division's management prepares a statement of major events that could be expected to materially affect the Division's budget and provides initial estimates of budget increases or decreases associated with those events.

In addition, the Office of the Controller prepares a "current level of operation" budget target. This target takes into account known or anticipated factors such as the planned federal government general pay increase, retirement costs, hospital and medical costs, inflation, etc., and results in a projected increase in expenses over the current year estimate. Along with the Division's input, this current level forms the basis for further review and setting of the final guideline used for developing the budget. The Chairman of the Board approves the final guideline, which is then sent out to the Divisions for use in developing their budgets. The major responsibility for formulating budget requirements rests with the Program Managers. Program Managers undertake a comprehensive process starting with identifying new initiatives as well as reevaluating ongoing activities. The budget includes a description of the program's objectives and projects undertaken to accomplish objectives, the resources needed to accomplish objectives and projects, and an indication of the priority of each project.

The Program Managers forward their budget, in the form of decision packages, to Division management for evaluation and coordination. The administrative assistant in each Division reviews the submission for completeness and conformity to the Board's budget guidelines which allow Division management to focus attention on the substance of the requests.

Upon completion of the review session with all the Program Managers and agreement at the Division level on the level of activity and funding necessary for activities, the Division Director submits, in September, the Division's proposed budget to the Controller's office.

Capital Budget Process

Historically, the Board of Governors has followed the same accounting practices as the federal government; that is, it expenses rather than depreciates capital assets. However, it is now making the transition to GAAP (generally accepted accounting principles). This approach more closely resembles those of private sector concerns, rather than that of the federal government. The Reserve Banks currently follow GAAP.

An important part of the Board's planning and budget process is the planning and budgeting for major capital acquisitions. In the case of major building or renovation programs, such as the construction of the Martin Building in the early 1970s, a multi-year plan and budget were prepared and approved by the Board of Governors. Similarly, major purchases of large mainframe computers have occurred only after detailed cost/benefit analyses and lease/purchase analyses are prepared and reviewed.

The Board must approve all major capital acquisitions. In the case of smaller capital items, such as furniture and equipment, the various Divisions include in their budget their resource requests and these are reviewed during the normal budget process.

Centrally Provided Services

Because of the size of the Division of Data Processing's expenditures and the support characteristics of this Division's work, special processes have been established to plan, review and control data processing expenses. Each Division or Office at the Board that uses data processing resources must provide, as part of its budget submission, its expected use of data processing.

In addition to requests for anticipated data processing resource utilization, Divisions are requested to provide expected usage data to those Divisions with responsibility to provide specific services. (For example, all books are budgeted in the libraries of the Research and Statistics and Legal

Divisions.) These data allow the Division providing the services to prepare its own budget. The purpose of these requests is to ensure that centrally provided services are budgeted in accordance with the expected pattern of use.

Board Review Process

Division budgets are reviewed at various management levels. The Controller's Office analyzes each Division's submission to determine that the cost justification is adequate, that objectives are consistent with the Division mission and goals, and that the proposed resource levels are appropriate for effective and efficient accomplishment of objectives. Technical questions and initial revisions for change are handled between the Controller's Office and the Division. Key issues are identified for further discussion. The Controller's Office and the Staff Director for Management hold budget meetings with each Division Director to communicate their analysis, request further information, if necessary, and receive answers to questions raised. These meetings usually result in reductions to Division budget. Each Division budget, as adjusted, is then reviewed with the Administrative Governor or the appropriate Board Oversight Committee.

Board Approval

A consolidated budget document is prepared and submitted to the Chairman via the Administrative Governor prior to the Board's full consideration. This review often results in further reductions to Division budgets. In early December, the Controller's Office prepares the Board budget for review and approval by the Board of Governors at a public Board meeting. An official record of the Board's budget (the Official Budget Book) is prepared summarizing Division objectives, initial budget submissions, changes made during budget reviews, and the approved budget.

The Monitoring and Control Process

Board expenses are monitored and reviewed throughout the budget year by all levels of Board management. To facilitate this monitoring, each Division at the beginning of the year allocates its approved budget into quarterly plans, which show by quarter, the funding for each object and sub-object class of expenditure in each program. The Office of the Controller produces reports throughout the budget year to the lowest level of accounting detail. The Office of the Controller uses these reports to monitor actual performance against budgeted targets and alert management on a timely basis of any problems.

Formal performance reports are submitted to the Board on a quarterly basis. Each July Division budgets as of June 30 are formally reviewed in meetings with the Controller and the Staff Director for Management. Prior to the meetings, projections for the remainder of the year are made by the Office of the Controller and discussed with administrative personnel from the Divisions. Significant changes to the original budget must be approved by the Board or by management (below the Board level) under delegated authority. Early in the following year, a comprehensive report discussing the previous year's performance employment and expense trends, and attainment of objectives, is presented to the Board for review.

Requests for changes to budget are very carefully evaluated by the Controller's Office, and in most cases, by the Staff Director for Management. The review process is similar to the budget review process. Of course only very significant and important resource problems are dealt with by changing approved budgets. In most cases, Divisions must find offsetting decreases to fund unanticipated needs.

Federal Reserve

Summary
Expense Reports by
F.R. District

1985 PACS EXPENSE REPORT

Division of Federal Reserve Bank Operations

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Board of Governors of the Federal Reserve System

FEDERAL RESERVE DISTRICT	TOTAL EXPENSE		REIMBURSEMENTS		NET EXPENSE		AVERAGE NUMBER OF PERSONNEL	
	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	NUMBER	% CHANGE FROM YEAR AGO
BOSTON	15,948,087	5.94	917,959	6.08	15,030,128	5.93	1,427.39	4.28
NEW YORK	52,046,278	-0.17	5,022,376	6.14	47,023,902	-0.79	4,256.11	0.23
PHILADELPHIA	14,186,290	5.99	1,900,385	36.07	12,285,905	2.49	1,136.22	1.62
CLEVELAND	15,607,455	1.67	1,312,155	-3.13	14,295,300	2.14	1,392.03	0.80
RICHMOND	21,192,087	5.10	1,408,405	-9.85	19,783,682	6.35	1,936.70	2.18
ATLANTA	24,239,693	6.77	1,432,044	9.47	22,807,649	6.60	2,104.59	4.66
CHICAGO	31,574,879	-5.18	2,469,535	2.69	29,105,344	-5.75	2,769.34	-8.35
ST. LOUIS	13,783,445	-0.41	1,384,898	16.90	12,398,547	-2.03	1,251.97	-0.93
MINNEAPOLIS	13,392,567	1.22	608,392	-3.05	12,784,175	1.43	1,109.46	-3.21
KANSAS CITY	17,266,074	1.03	1,149,673	1.51	16,116,401	1.00	1,575.84	-0.77
DALLAS	17,378,807	10.53	833,821	-25.41	16,544,986	13.28	1,454.83	3.57
SAN FRANCISCO	31,021,635	7.91	2,327,236	0.11	28,694,399	8.59	2,323.14	2.67
SYSTEM TOTAL	267,637,297	2.66	20,766,879	3.78	246,870,418	2.56	22,739.62	0.13

FEDERAL RESERVE DISTRICT	PERSONNEL		MATERIALS AND SUPPLIES		EQUIPMENT		SHIPPING	
	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO
BOSTON	11,081,303	8.10	538,319	11.97	1,816,222	44.08	831,466	-.64
NEW YORK	34,855,872	1.75	1,874,994	-6.65	5,895,427	5.14	2,148,922	-24.06
PHILADELPHIA	8,635,469	4.66	569,463	-3.49	1,299,644	10.33	1,069,788	-4.29
CLEVELAND	10,297,818	7.01	659,046	4.57	2,018,738	9.92	1,439,602	-3.64
RICHMOND	12,844,725	5.23	967,474	3.94	2,836,401	30.37	1,646,969	-22.27
ATLANTA	14,734,801	5.03	1,012,680	11.90	3,181,339	10.69	2,314,003	-.56
CHICAGO	20,690,173	-5.17	1,103,431	-12.91	5,132,906	8.89	2,071,190	-16.29
ST LOUIS	8,854,407	.25	656,719	1.79	1,463,451	10.76	1,193,810	-18.48
MINNEAPOLIS	7,844,300	-.96	432,282	1.06	1,540,287	5.82	1,280,788	11.30
KANSAS CITY	11,279,426	1.41	760,317	-1.17	1,956,259	-.91	1,514,363	-14.47
DALLAS	11,038,609	8.97	686,385	14.17	2,628,674	8.29	1,606,223	1.42
SAN FRANCISCO	19,425,101	6.04	1,022,863	11.55	4,133,987	15.81	3,099,648	9.76
SYSTEM TOTAL	171,582,412	2.98	10,263,933	1.07	33,059,295	11.55	20,216,764	-8.07

FEDERAL RESERVE DISTRICT	TRAVEL		COMMUNICATIONS		BUILDING		OTHER	
	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO
BOSTON	189,095	19.57	239,297	-10.01	2,324,931	3.09	1,021,637	45.62
NEW YORK	497,131	-11.56	849,126	-9.45	4,573,492	-2.93	1,216,817	6.94
PHILADELPHIA	187,190	53.94	183,424	4.36	1,640,138	3.10	573,718	68.56
CLEVELAND	284,374	-12.00	163,927	-19.22	1,095,054	1.56	744,355	14.18
RICHMOND	357,691	24.72	282,640	2.94	2,324,652	7.26	668,620	9.94
ATLANTA	374,377	18.38	423,432	-.98	1,275,198	15.53	1,230,638	.04
CHICAGO	589,570	2.37	333,376	-11.26	2,622,718	5.10	1,385,756	-17.37
ST LOUIS	189,888	22.36	176,120	16.18	799,784	4.90	488,206	13.02
MINNEAPOLIS	200,801	7.31	133,406	-35.78	1,263,761	-3.68	494,080	.76
KANSAS CITY	296,297	-9.98	276,862	1.17	968,242	7.92	470,291	4.16
DALLAS	338,097	15.86	229,469	11.55	1,094,412	5.09	642,061	16.93
SAN FRANCISCO	487,477	-1.13	396,522	-16.39	2,283,441	11.07	1,118,508	4.22
SYSTEM TOTAL	3,991,984	5.05	3,567,601	-7.14	22,265,823	3.82	9,974,647	7.74

FEDERAL RESERVE DISTRICT	RECOVERIES		CONTRA EXPENSE		SHARED COST DISTRIBUTED		SHARED COST RECEIVED	
	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO	AMOUNT	% CHANGE FROM YEAR AGO
BOSTON	-1,881,056	39.19	-50,558	157.70	-1,093,870	165.94	538,901	49.91
NEW YORK	-560,802	5.41	-1,158	-28.43	-313,998	11.78	1,010,055	12.94
PHILADELPHIA	-465,667	82.54	-881	136.03		-100.00	493,612	36.01
CLEVELAND	-742,901	83.40	-63,698	15.92	-833,202	97.75	588,342	39.09
RICHMOND	-931,529	11.66	-77,227	48.45	-347,351	110.92	659,119	35.45
ATLANTA	-376,992	26.16	-83,155	22.77	-561,656	-13.25	715,028	39.46
CHICAGO	-612,733	8.72	-192,866	7.73	-2,485,234	18.70	1,016,592	23.87
ST LOUIS	-382,112	22.28	-12,229	13.77	-211,122	814.15	526,527	35.08
MINNEAPOLIS	-173,326	-14.59	-16,138	31.79	-28,713		421,187	44.02
KANSAS CITY	-260,216	-4.57	-207,691	20.26	-390,872	-22.68	602,796	32.94
DALLAS	-487,987	5.10	-95,897	77.52	-887,676	-12.33	618,438	37.11
SAN FRANCISCO	-863,786	-11.07	-16,936	-23.86	-812,178	138.38	826,980	36.89
SYSTEM TOTAL	-7,298,727	18.88	-786,830	27.29	-7,965,464	32.07	7,965,457	32.47

FEDERAL RESERVE DISTRICT	TOTAL EXPENSE	
	AMOUNT	% CHANGE FROM YEAR AGO
BOSTON	15,948,087	5.94
NEW YORK	52,046,278	-.17
PHILADELPHIA	14,186,290	5.99
CLEVELAND	15,607,455	1.67
RICHMOND	21,192,086	5.10
ATLANTA	24,239,693	6.77
CHICAGO	31,574,079	-5.14
ST LOUIS	13,783,445	-.41
MINNEAPOLIS	13,392,567	1.22
KANSAS CITY	17,266,074	1.03
DALLAS	17,378,808	10.53
SAN FRANCISCO	31,021,635	7.91
SYSTEM TOTAL	267,637,295	2.44

SERVICE LINE:	MONETARY & ECONOMIC POLICY - 1980				U.S. TREAS & GOVT AGENCIES - 1980			
FEDERAL RESERVE DISTRICT	TOTAL COST	% CHANGE FROM YEAR AGO	REIMBURSE-MENTS	NET COST	TOTAL COST	% CHANGE FROM YEAR AGO	REIMBURSE-MENTS	NET COST
BOSTON	1,333,308	-25.68		1,333,308	1,696,237	8.88	917,676	778,561
NEW YORK	6,986,215	-5.09	157,898	6,828,317	7,103,919	3.91	4,651,167	2,452,752
PHILADELPHIA	1,266,175	-12.80		1,266,175	2,760,104	32.27	1,898,513	861,591
CLEVELAND	1,006,010	-21.00		1,006,010	2,037,181	-4.86	1,312,156	725,025
RICHMOND	1,133,039	-27.26		1,133,039	2,112,069	4.44	1,404,580	707,489
ATLANTA	1,790,482	-12.44		1,790,482	2,229,901	1.00	1,429,021	800,880
CHICAGO	1,791,166	-16.90		1,791,166	3,727,286	-6.30	2,467,072	1,260,214
ST. LOUIS	1,170,773	-26.19		1,170,773	1,820,335	0.15	1,072,161	748,174
MINNEAPOLIS	991,070	-13.08		991,070	988,366	-12.58	596,063	392,303
KANSAS CITY	1,283,040	-10.32		1,283,040	1,760,238	-0.09	1,136,290	623,948
DALLAS	1,253,558	-19.61		1,253,558	1,518,467	-3.38	833,821	684,646
SAN FRANCISCO	2,389,902	-11.31		2,389,902	3,569,601	-4.91	2,327,235	1,242,366
SYSTEM TOTAL	22,404,358	-16.13	157,898	22,246,460	31,323,704	2.01	20,045,755	11,277,949

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 1980				SUPERVISION & REGULATION - 1980			
FEDERAL RESERVE DISTRICT	TOTAL COST	% CHANGE FROM YEAR AGO	REIMBURSE-MENTS	NET COST	TOTAL COST	% CHANGE FROM YEAR AGO	REIMBURSE-MENTS	NET COST
BOSTON	11,024,812	8.00	283	11,024,529	1,893,690	19.76		1,893,690
NEW YORK	31,300,537	-0.04	213,311	31,087,226	6,655,627	0.50		6,655,627
PHILADELPHIA	8,357,177	2.60	1,872	8,355,305	1,802,041	5.97		1,802,041
CLEVELAND	10,720,499	7.32		10,720,499	1,843,012	-5.82		1,843,012
RICHMOND	15,667,534	8.80	3,805	15,663,729	2,278,579	3.04		2,278,579
ATLANTA	17,360,745	9.11	3,023	17,357,722	2,054,565	11.73		2,054,565
CHICAGO	20,808,759	-7.00		20,808,759	5,207,667	0.82	2,463	5,205,204
ST. LOUIS	9,179,790	1.40	312,734	8,867,056	1,600,579	5.86		1,600,579
MINNEAPOLIS	9,424,030	3.46	12,349	9,411,681	1,909,120	7.99		1,909,120
KANSAS CITY	11,409,050	2.97	12,584	11,396,466	2,012,130	2.20		2,012,130
DALLAS	11,904,891	14.60		11,904,891	2,701,909	22.60		2,701,909
SAN FRANCISCO	20,735,520	11.69		20,735,520	4,326,623	15.84		4,326,623
SYSTEM TOTAL	177,894,104	6.30	560,761	177,333,343	36,015,160	7.56	2,463	36,012,697

FEDERAL RESERVE DISTRICT	TOTAL COST
BOSTON	15,948,087
NEW YORK	52,046,308
PHILADELPHIA	14,186,297
CLEVELAND	15,607,502
RICHMOND	21,192,041
ATLANTA	24,239,693
CHICAGO	31,574,858
ST. LOUIS	13,783,477
MINNEAPOLIS	13,392,574
KANSAS CITY	17,266,058
DALLAS	17,378,825
SAN FRANCISCO	31,021,646
SYSTEM TOTAL	267,637,366

SERVICE LINE:	MONETARY & ECONOMIC POLICY - 1000				MONETARY & ECONOMIC POLICY - 1000			
SERVICE:	ECONOMIC POLICY DETERMINATION - 1300				ECONOMIC POLICY DETERMINATION - 1300			
ACTIVITY:	CURRENT ECONOMIC ANALYSIS - 1302				LONG RANGE ECONOMIC RESEARCH - 1304			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	82,245			82,648	208,701			210,901
NEW YORK	1,497,648			1,497,648	268,379			268,379
PHILADELPHIA	132,483			132,483	232,672			232,672
CLEVELAND	216,148			216,148	120,275			120,275
RICHMOND	162,765			162,765	143,946			143,946
ATLANTA	156,227			156,227	227,568			227,568
CHICAGO	370,870			372,818	195,041			195,675
ST. LOUIS	179,473			179,473	229,933			229,933
MINNEAPOLIS	104,339			104,339	388,796			388,796
KANSAS CITY	136,203			136,203	222,533			222,533
DALLAS	274,678			274,678	160,045			160,045
SAN FRANCISCO	198,475			198,475	292,084			292,084
SYSTEM TOTAL	3,511,554			3,513,905	2,689,973			2,692,807

SERVICE LINE:	MONETARY & ECONOMIC POLICY - 1000				MONETARY & ECONOMIC POLICY - 1000			
SERVICE:	ECONOMIC POLICY DETERMINATION - 1300				ECONOMIC POLICY DETERMINATION - 1300			
ACTIVITY:	SYSTEM-INITIATED DATA REPORTING - 1305				BANK-INITIATED DATA REPORTING - 1307			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	323,531			409,930	10,340			10,985
NEW YORK	1,476,738			1,476,798	54,224			54,224
PHILADELPHIA	393,695			399,587	2,960			2,960
CLEVELAND	189,003			189,003				
RICHMOND	289,620			294,310				
ATLANTA	621,891			621,913	1,872			1,872
CHICAGO	649,966			651,798	57			61
ST. LOUIS	315,365			315,365	4,354			4,354
MINNEAPOLIS	143,688			143,644	78			78
KANSAS CITY	447,787			447,844	21,398			21,398
DALLAS	275,640			275,640	4,352			4,352
SAN FRANCISCO	990,143			1,003,021				
SYSTEM TOTAL	6,117,075			6,228,853	99,635			100,284

SERVICE LINE:	MONETARY & ECONOMIC POLICY - 1000					MONETARY & ECONOMIC POLICY - 1000			
SERVICE:	ECONOMIC POLICY DETERMINATION - 1500				TOTAL	OPEN MARKET TRADING - 1600			
ACTIVITY:						OPEN MARKET TRADING - 1600			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	240,221	370,699	1,333,348		1,333,348				
NEW YORK	145,768	877,197	4,520,010		4,520,010	1,067,375			1,067,375
PHILADELPHIA	148,695	349,770	1,266,175		1,266,175				
CLEVELAND	114,116	364,460	1,006,010		1,006,010				
RICHMOND	143,105	389,673	1,133,039		1,133,039				
ATLANTA	282,439	524,463	1,794,482		1,794,482				
CHICAGO	255,231	515,563	1,791,166		1,791,166				
ST. LOUIS	85,325	360,323	1,174,773		1,174,773				
MINNEAPOLIS	133,230	220,983	991,070		991,070				
KANSAS CITY	87,750	368,112	1,283,840		1,283,840				
DALLAS	177,285	361,550	1,253,558		1,253,558				
SAN FRANCISCO	247,155	649,167	2,389,902		2,389,902				
SYSTEM TOTAL	2,060,368	5,341,988	19,938,153		19,938,153	1,067,375			1,067,375

SERVICE LINE:	MONETARY & ECONOMIC POLICY - 1000					MONETARY & ECONOMIC POLICY - 1000		
SERVICE:	OPEN MARKET TRADING - 1600				TOTAL	TOTAL		
ACTIVITY:								
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON						1,333,348		1,333,348
NEW YORK	17,626	501,208	2,466,205	157,898	2,308,307	6,986,215	157,898	6,828,317
PHILADELPHIA						1,266,175		1,266,175
CLEVELAND						1,006,010		1,006,010
RICHMOND						1,133,039		1,133,039
ATLANTA						1,794,482		1,794,482
CHICAGO						1,791,166		1,791,166
ST. LOUIS						1,174,773		1,174,773
MINNEAPOLIS						991,070		991,070
KANSAS CITY						1,283,840		1,283,840
DALLAS						1,253,558		1,253,558
SAN FRANCISCO						2,389,902		2,389,902
SYSTEM TOTAL	17,626	501,208	2,466,205	157,898	2,308,307	22,404,358	157,898	22,246,460

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000				U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	SAVINGS BONDS - 2100				SAVINGS BONDS - 2100			
ACTIVITY:	ORIGINAL ISSUE - 2101				ACCOUNTING FOR STOCK - 2103			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	48,142	0.24	11.29	50,561	106,850	3.74	24.80	107,053
NEW YORK	148,513	0.17	-3.86	148,513	382,596	5.43	-2.52	382,596
PHILADELPHIA	58,358	0.21	2.26	58,358	109,902	3.76	-13.23	109,902
CLEVELAND	131,533	0.23	16.15	131,533	141,302	3.84	-9.40	141,302
RICHMOND	52,906	0.23	49.58	52,906	163,189	3.93	-4.00	163,189
ATLANTA	69,297	0.14	-32.99	69,297	167,032	3.84	10.58	167,399
CHICAGO	147,501	0.26	-9.69	147,854	282,300	4.75	-2.52	283,010
ST. LOUIS	24,762	0.58	-30.67	24,762	114,597	4.67	11.81	114,597
MINNEAPOLIS	39,770	0.31	-15.19	39,770	69,987	3.42	-21.20	69,987
KANSAS CITY	46,420	0.37	-12.19	76,071	112,515	3.92	3.98	112,515
DALLAS	21,935	0.11	-29.22	21,935	107,671	4.08	-30.37	107,671
SAN FRANCISCO	119,092	0.27	-11.54	120,109	295,143	4.38	5.63	296,340
SYSTEM TOTAL	908,229	0.22	-4.36	941,669	2,053,088	4.30	-2.18	2,055,561

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000				U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	SAVINGS BONDS - 2100				SAVINGS BONDS - 2100			
ACTIVITY:	REISSUES & REPLACEMENTS - 2104				DIRECT REDEMPTIONS - 2106			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	36,220	0.68	16.93	36,220	58,323	0.92	0.30	58,525
NEW YORK	127,524	0.74	7.47	127,524	210,239	1.40	35.94	210,239
PHILADELPHIA	48,605	0.60	-6.05	48,605	73,222	1.00	-6.42	73,222
CLEVELAND	92,079	0.30	33.86	92,079	91,449	0.99	3.52	91,449
RICHMOND	47,423	0.91	27.17	47,423	66,912	1.28	19.38	66,958
ATLANTA	45,784	0.89	13.65	45,784	78,366	1.02	26.44	78,735
CHICAGO	145,376	0.79	2.60	145,692	213,840	1.24	-6.92	214,345
ST. LOUIS	39,008	0.93	59.43	39,008	42,952	0.95	23.51	42,952
MINNEAPOLIS	36,923	0.77	-25.61	36,923	51,585	1.37	-4.79	51,585
KANSAS CITY	32,029	0.59	-8.98	60,617	62,958	0.85	56.45	91,633
DALLAS	26,487	0.15	17.14	26,487	37,769	1.07	39.28	37,769
SAN FRANCISCO	70,064	1.16	-8.49	71,081	111,960	1.38	-20.82	113,295
SYSTEM TOTAL	747,522	0.62	10.85	777,443	1,099,575	1.15	9.83	1,130,707

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000				U.S. TREAS & GOVT AGENCIES - 2000				
SERVICE:	SAVINGS BONDS - 2100				SAVINGS BONDS - 2100				
ACTIVITY:	PROCESSING RETIRED BONDS - 2108				TOTAL				
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
		AMOUNT	% CHANGE FROM YEAR AGO						
BOSTON	45,745	1.16	15.58	46,399	49,579	187,182	535,519	298,760	236,759
NEW YORK	167,943	1.05	21.27	167,983	10,005	357,794	1,404,694	1,036,812	367,882
PHILADELPHIA	80,028	1.51	8.53	80,028	13,840	176,015	559,990	370,135	189,855
CLEVELAND	81,279	1.03	8.61	81,279	16,716	285,244	839,600	537,639	301,961
RICHMOND	92,964	1.90	-4.65	93,087	18,832	200,125	642,520	423,566	218,954
ATLANTA	74,436	1.21	11.31	74,436	53,663	231,021	721,135	435,649	285,486
CHICAGO	135,927	1.02	7.28	136,252	64,169	431,913	1,423,235	952,416	470,819
ST. LOUIS	50,719	1.33	41.32	50,719	11,974	158,121	442,173	271,968	170,205
MINNEAPOLIS	31,481	1.04	-12.87	31,481	26,920	105,910	362,576	224,083	138,493
KANSAS CITY	56,905	1.13	-9.44	57,108	14,152	201,758	613,934	397,468	216,466
DALLAS	59,665	0.98	-12.08	59,665	23,207	147,428	424,102	253,468	170,634
SAN FRANCISCO	152,710	1.32	-26.23	154,109	13,037	375,327	1,143,298	738,809	404,489
SYSTEM TOTAL	1,029,882	1.24	0.03	1,032,586	316,172	2,858,638	9,112,776	5,940,773	3,172,003

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000				U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	OTHER TREASURY ISSUES - 2200				OTHER TREASURY ISSUES - 2200			
ACTIVITY:	ORIGINAL ISSUE - 2202				SERVICING - 2205			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	146,624	8.90	27.14	147,380	48,327	14.77	80.59	49,436
NEW YORK	817,579	17.26	38.30	818,360	553,347	21.28	-1.22	553,347
PHILADELPHIA	138,618	13.41	40.63	144,510	76,645	28.47	17.19	76,645
CLEVELAND	119,545	9.82	32.72	119,545	69,966	20.23	0.97	69,966
RICHMOND	107,471	12.29	25.36	107,647	53,585	20.38	3.89	53,660
ATLANTA	97,399	8.59	50.35	97,399	56,762	13.01	-15.77	56,762
CHICAGO	297,131	11.78	47.67	297,623	167,626	19.27	13.59	167,967
ST. LOUIS	94,634	12.09	28.17	120,918	131,828	16.06	89.83	131,828
MINNEAPOLIS	73,514	12.20	17.35	73,514	31,322	31.26	64.32	31,322
KANSAS CITY	129,074	11.78	30.14	132,322	40,484	21.22	-0.11	42,086
DALLAS	60,827	9.30	40.03	60,827	21,607	32.11	87.15	21,607
SAN FRANCISCO	251,280	9.66	11.56	305,050	83,634	20.76	5.40	84,312
SYSTEM TOTAL	2,333,696	12.35	31.57	2,425,095	1,335,053	20.22	12.33	1,338,938

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000				U.S. TREAS & GOVT AGENCIES - 2000				
SERVICE:	OTHER TREASURY ISSUES - 2200				OTHER TREASURY ISSUES - 2200				TOTAL
ACTIVITY:	REGISTERING - 2208								
		UNIT PRODUCTION COST							
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSEMENTS	NET COST
BOSTON	54,241	4.41	8.23	55,099	99,426	141,615	492,956	251,913	241,043
NEW YORK	296,757	10.16	3.30	296,757	20,535	560,773	2,249,772	1,667,934	581,838
PHILADELPHIA	100,320	8.61	12.47	100,320	16,590	130,818	476,883	321,475	155,408
CLEVELAND	58,584	4.19	9.05	58,584	21,236	164,030	433,361	248,089	185,272
RICHMOND	40,994	5.47	34.06	41,067	39,623	147,363	389,360	202,367	186,993
ATLANTA	69,216	4.01	28.07	69,583	59,373	104,182	387,299	223,744	163,555
CHICAGO	152,548	4.87	17.59	152,921	57,094	249,598	925,203	626,592	298,611
ST. LOUIS	47,976	6.82	21.51	47,976	16,909	162,894	480,525	300,715	179,810
MINNEAPOLIS	22,318	11.38	23.79	22,318	49,755	50,853	222,762	125,201	97,561
KANSAS CITY	60,239	4.04	15.88	62,811	14,586	150,009	401,814	231,538	170,276
DALLAS	20,396	2.96	34.68	20,396	11,767	74,625	189,222	102,827	86,395
SAN FRANCISCO	80,805	8.96	36.86	81,134	18,697	303,254	792,447	459,006	333,441
SYSTEM TOTAL	1,004,386	6.67	15.91	1,008,966	420,591	2,240,014	7,441,604	4,761,401	2,680,203

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000				U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	CENTRALLY PROVIDED TREAS & AGENCY SVC - 2250				CENTRALLY PROVIDED TREAS & AGENCY SVC - 2250			
ACTIVITY:	TREAS DIRECT-ACCESS BOOK-ENTRY SYS OPER - 2252				TREAS DIRECT-ACCESS B-E PROCESSING - 2254			
		UNIT PRODUCTION COST				UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON					1			1
NEW YORK								
PHILADELPHIA	201,520			883,532				
CLEVELAND								
RICHMOND								
ATLANTA								
CHICAGO					1			1
ST. LOUIS								
MINNEAPOLIS								
KANSAS CITY								
DALLAS								
SAN FRANCISCO								
SYSTEM TOTAL	201,520			883,532	2			2

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000					U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	CENTRALLY PROVIDED TREAS & AGENCY SVC - 2250 TOTAL					GOVERNMENT AGENCY ISSUES - 2300			
ACTIVITY:						GOVERNMENT AGENCY ISSUES - 2303			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON			1		1	24,194			26,715
NEW YORK		11,441	11,441		11,441	754,276			754,276
PHILADELPHIA	50,612	204,217	1,218,361	909,783	308,578	23,496			23,496
CLEVELAND						29,018			29,018
RICHMOND		2,566	2,566		2,566	48,607			48,677
ATLANTA						66,744			66,744
CHICAGO			1		1	28,657			28,699
ST. LOUIS						32,253			32,253
MINNEAPOLIS						4,003			4,003
KANSAS CITY						17,488			21,053
DALLAS						28,320			28,320
SAN FRANCISCO						61,653			64,181
SYSTEM TOTAL	50,612	218,224	1,232,370	909,783	322,587	1,119,509			1,120,235

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000					U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	GOVERNMENT AGENCY ISSUES - 2300 TOTAL					OTHER TREAS & GOVERNMENT AGENCY SERVICES - 2400			
ACTIVITY:						OTHER TREASURY & GOV'T AGENCY SERVICES - 2403			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	43,555	18,118	88,388	88,389	-1	63,523			64,064
NEW YORK	10,175	280,085	1,044,536	1,035,741	8,795	1,054,611			1,054,799
PHILADELPHIA	3,196	6,706	35,398	31,487	3,911	51,791			51,791
CLEVELAND	18,056	17,241	56,315	56,319	-4	39,414			39,418
RICHMOND	24,988	37,642	101,303	101,059	244	174,219			174,356
ATLANTA	29,994	29,738	126,476	154,197	-27,721	115,368			115,368
CHICAGO	9,577	16,592	54,868	52,312	2,556	161,544			161,813
ST. LOUIS	5,851	37,687	75,791	61,208	14,583	60,237			60,237
MINNEAPOLIS	21,128	5,610	31,523	25,139	6,384	29,501			29,501
KANSAS CITY	4,629	14,457	40,139	38,556	1,583	53,561			54,112
DALLAS	6,383	18,763	53,386	35,480	17,906	80,687			80,687
SAN FRANCISCO	8,050	20,684	92,837	100,530	-7,693	176,192			176,874
SYSTEM TOTAL	177,490	495,245	1,808,970	1,780,417	28,553	2,060,568			2,062,936

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000					U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	OTHER TREAS & GOVERNMENT AGENCY SERVICES - 2400 TOTAL					TREASURY & GOVERNMENT AGENCY COUPONS - 2500			
ACTIVITY:						COUPON PROCESSING - 2504			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	15,969	35,886	115,914	5,545	110,369	10,208	692.12	-0.64	10,208
NEW YORK	10,672	266,293	1,331,764	50,645	1,281,119	125,850	361.03	68.29	125,850
PHILADELPHIA	2,327	15,417	69,535	2,104	67,431	46,060	616.13	41.15	46,060
CLEVELAND	2,961	20,015	65,890	11,431	54,459	39,262	755.06	28.38	39,262
RICHMOND	10,338	99,639	284,333	193,292	91,041	26,228	936.71	38.12	26,362
ATLANTA	17,100	51,627	184,095	18,543	165,552	48,716	919.17	61.10	48,716
CHICAGO	13,947	64,913	240,673	38,711	201,962	75,313	731.19	34.39	75,559
ST. LOUIS	2,018	48,380	111,435	18,005	93,430	28,161	694.05	31.34	28,161
MINNEAPOLIS	5,924	17,085	52,510	18,130	34,380	9,756	975.60	-5.20	9,756
KANSAS CITY	2,468	23,661	80,241	56,093	24,148	62,479	1,633.81	58.32	62,736
DALLAS	6,095	60,722	148,224	16,560	131,664	13,992	823.06	67.08	13,992
SAN FRANCISCO	4,136	64,149	245,159	59,903	185,256	57,175	952.93	2.28	57,430
SYSTEM TOTAL	95,050	771,787	2,929,773	480,962	2,448,811	531,290	715.90	37.93	532,092

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000					U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	TREASURY & GOVERNMENT AGENCY COUPONS - 2500 TOTAL					FOOD COUPONS - 2600			
ACTIVITY:						FOOD COUPON OPERATIONS - 2603			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	3,180	21,197	42,585	19,328	23,257	75,914	3.41	32.85	75,914
NEW YORK	1,208	39,379	166,437	131,782	34,655	202,689	2.50	-1.31	202,689
PHILADELPHIA	1,658	48,718	88,428	31,266	57,162	77,859	2.78	26.04	77,859
CLEVELAND	1,234	42,129	82,625	39,856	42,769	145,568	2.43	15.22	143,568
RICHMOND	463	23,894	50,719	27,254	23,465	175,250	2.88	13.53	175,573
ATLANTA	5,982	25,799	80,497	50,503	29,994	194,809	2.03	3.84	195,178
CHICAGO	6,139	36,785	118,483	73,884	44,599	282,709	3.19	20.93	283,325
ST. LOUIS	1,365	31,685	61,191	22,955	38,236	115,172	2.99	0.21	115,172
MINNEAPOLIS	1,154	16,365	27,275	13,721	13,554	57,924	4.05	7.81	57,924
KANSAS CITY	1,551	32,653	76,740	38,105	38,635	120,862	3.96	-4.94	120,938
DALLAS	784	9,344	24,122	18,473	5,649	129,416	2.85	5.62	129,416
SAN FRANCISCO	1,071	55,962	114,463	59,399	55,064	290,178	3.50	29.48	291,642
SYSTEM TOTAL	25,771	375,962	933,765	526,526	407,239	1,876,362	2.85	12.70	1,879,198

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000					U.S. TREAS & GOVT AGENCIES - 2000			
SERVICE:	FOOD COUPONS - 2600				TOTAL	GOVERNMENT ACCOUNTS - 2700			
ACTIVITY:						FEDERAL TAXES & T.T.&L. ACCOUNTING - 2703			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	12,683	37,538	126,131	126,132	-1	98,832	0.71	-15.30	127,609
NEW YORK	1,784	123,544	328,017	327,420	597	317,006	2.38	3.05	322,835
PHILADELPHIA	2,848	38,585	119,292	119,292		112,971	1.33	56.64	112,971
CLEVELAND	4,372	109,539	259,479	259,513	-34	159,311	1.23	13.82	159,311
RICHMOND	2,043	87,557	265,973	265,431	542	173,091	1.03	20.52	191,639
ATLANTA	23,909	99,935	319,022	332,586	-13,564	212,252	0.67	18.99	213,799
CHICAGO	17,332	106,789	407,366	400,479	6,887	318,197	0.85	2.26	318,987
ST. LOUIS	5,144	115,160	235,476	198,550	36,926	158,058	0.89	-8.45	198,760
MINNEAPOLIS	5,205	48,227	107,356	104,170	3,186	89,205	0.60	1.80	89,205
KANSAS CITY	4,691	82,884	216,513	207,130	9,383	175,068	0.70	1.85	178,868
DALLAS	6,517	94,499	230,432	160,028	70,404	229,662	0.56	-8.21	246,985
SAN FRANCISCO	4,121	161,488	437,211	449,534	-12,323	434,184	0.95	-8.28	459,974
SYSTEM TOTAL	91,449	1,081,621	3,052,268	2,950,265	102,003	2,470,937	0.89	1.98	2,620,903

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000				U.S. TREAS & GOVT AGENCIES - 2000				
SERVICE:	GOVERNMENT ACCOUNTS - 2700				GOVERNMENT ACCOUNTS - 2700				TOTAL
ACTIVITY:	TREA.'S GEN & GOV'T AGENCY ACC'T PROC - 2708								
		UNIT PRODUCTION COST							
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON	14,254	1.01	0.83	14,254	70,611	82,069	294,743	127,609	167,134
NEW YORK	74,127	0.84	-19.47	74,127	7,492	162,884	567,258	400,833	166,425
PHILADELPHIA	8,817	0.65	14.25	8,817	7,206	63,223	192,217	112,971	79,246
CLEVELAND	18,303	1.33	18.92	18,383	16,528	105,763	299,911	159,309	140,602
RICHMOND	30,463	1.54	-22.29	30,529	35,223	117,934	375,315	191,631	183,684
ATLANTA	26,495	1.12	35.77	26,495	55,326	115,757	411,377	213,799	197,578
CHICAGO	24,989	1.34	52.21	25,040	38,469	179,001	557,457	322,678	234,779
ST. LOUIS	22,244	1.77	48.87	22,248	14,685	178,055	413,744	198,760	214,984
MINNEAPOLIS	6,791	1.01	29.03	6,791	35,633	52,705	184,334	85,599	98,735
KANSAS CITY	26,439	1.57	26.59	26,477	12,223	112,889	330,657	167,400	163,257
DALLAS	16,137	1.06	6.46	16,137	23,854	162,003	448,979	246,985	201,994
SAN FRANCISCO	45,898	1.03	31.08	46,170	17,618	220,428	744,186	460,054	284,132
SYSTEM TOTAL	314,957	1.09	11.31	315,508	331,068	1,552,619	4,820,178	2,687,628	2,132,550

SERVICE LINE:	U.S. TREAS & GOVT AGENCIES - 2000		
SERVICE:	TOTAL		
ACTIVITY:			
FEDERAL RESERVE DISTRICT	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON	1,696,237	917,676	778,561
NEW YORK	7,103,919	4,651,167	2,452,752
PHILADELPHIA	2,760,104	1,898,513	861,591
CLEVELAND	2,037,181	1,312,156	725,025
RICHMOND	2,112,089	1,404,600	707,489
ATLANTA	2,229,901	1,429,021	800,880
CHICAGO	3,727,286	2,467,072	1,260,214
ST. LOUIS	1,820,335	1,072,161	748,174
MINNEAPOLIS	988,346	596,043	392,303
KANSAS CITY	1,760,238	1,136,290	623,948
DALLAS	1,518,467	833,821	684,646
SAN FRANCISCO	3,569,601	2,327,235	1,242,366
SYSTEM TOTAL	31,323,704	20,045,755	11,277,949

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	SPECIAL CASH SERVICES - 3020				SPECIAL CASH SERVICES - 3020			
ACTIVITY:	CASH TRANSPORTATION - 3021				COIN WRAPPING - 3024			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	6,297			6,297	93,318	2.33		93,318
NEW YORK								
PHILADELPHIA	276,006			276,006	11,224			11,224
CLEVELAND	284,605			284,605	75,878	1.52		75,878
RICHMOND	1,115			1,115				
ATLANTA	8,182			8,182				
CHICAGO	27,496			27,496	92,135	2.80		92,135
ST. LOUIS	51,405			51,405				
MINNEAPOLIS	377,268			377,268	27,628	2.42		27,628
KANSAS CITY	64,540			64,540				
DALLAS	481,253			481,253				
SAN FRANCISCO	1,643,948			1,643,948				
SYSTEM TOTAL	3,222,115			3,222,115	300,183	2.25		300,183

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	SPECIAL CASH SERVICES - 3020				SPECIAL CASH SERVICES - 3020				TOTAL
ACTIVITY:	OTHER CASH SERVICES - 3027								
		UNIT PRODUCTION COST							
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON					205	1,363	101,183		101,183
NEW YORK									
PHILADELPHIA					592	19,849	307,671		307,671
CLEVELAND					449	37,150	398,082		398,082
RICHMOND						75	1,190		1,190
ATLANTA					134	737	9,053		9,053
CHICAGO	9,321			9,321	404	14,150	143,514		143,514
ST. LOUIS						5,023	56,428		56,428
MINNEAPOLIS					1,581	21,660	428,137		428,137
KANSAS CITY					332	9,376	74,248		74,248
DALLAS	1,605			1,605	100	2,418	485,368		485,368
SAN FRANCISCO					532	23,317	1,667,797		1,667,797
SYSTEM TOTAL	10,926			10,926	4,329	135,118	3,672,671		3,672,671

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	CURRENCY - 3090				CURRENCY - 3090			
ACTIVITY:	HIGH-SPEED CURRENCY PROCESSING - 3091				PAYING & RECEIVING - 3092			
		UNIT PRODUCTION COST				UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	447,400	2.33	7.84	447,408	567,590	0.90	-5.65	766,179
NEW YORK	1,634,955	3.27	1.92	1,745,730	1,836,158	1.01	-33.18	2,802,934
PHILADELPHIA	593,460	2.05	13.12	598,887	389,551	0.86	-19.34	395,537
CLEVELAND	412,423	2.45	19.66	412,423	476,523	0.89	-29.70	476,523
RICHMOND	845,621	2.77	16.77	846,617	708,310	0.83	-38.04	709,434
ATLANTA	776,067	1.86	2.85	777,258	576,298	0.55	-9.80	578,663
CHICAGO	520,504	2.44	-6.12	520,852	707,738	0.78	-30.71	708,563
ST. LOUIS	319,298	2.62	6.63	319,290	232,791	0.86	-49.54	237,565
MINNEAPOLIS	121,225	2.23	-25.12	121,225	251,130	1.72	-41.43	251,130
KANSAS CITY	397,656	3.05	-0.50	397,656	299,852	0.80	-51.84	302,632
DALLAS	452,703	2.35	13.97	452,703	322,997	0.70	-57.46	322,997
SAN FRANCISCO	1,356,961	2.88	9.56	1,360,441	910,153	0.66	-55.72	954,402
SYSTEM TOTAL	7,877,465	2.65	6.35	8,000,442	7,287,091	0.83	-37.22	7,706,559

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	CURRENCY - 3090				CURRENCY - 3090			
ACTIVITY:	VERIFYING DEPOSITS - 3094				COIN CANCELLATION, VERIFICATION & DEST - 3099			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	148,755	2.12	-3.45	148,871	99,025	3.53	-19.98	99,025
NEW YORK	495,980	6.25	5.75	568,412	175,165	9.13	28.19	175,192
PHILADELPHIA	93,942	1.78	-46.95	93,942	44,036	13.72	35.86	44,036
CLEVELAND	48,626	1.49	-12.07	48,626	35,511	3.25	4.05	35,511
RICHMOND	76,056	1.23	-31.72	76,188	77,348	2.05	-35.00	77,467
ATLANTA	5,673	0.86	-60.53	5,673	71,976	3.47	-16.76	72,345
CHICAGO	290,270	1.49	3.61	290,379	41,158	6.58	12.88	41,166
ST. LOUIS	248		-100.00	248	25,341	7.31	-26.85	25,341
MINNEAPOLIS	47,061	3.04	6.47	47,861	25,128	5.62	2.63	25,128
KANSAS CITY	63,785	3.51	9.79	64,001	53,005	3.42	-6.82	54,179
DALLAS	1,579	17.54	40.74	1,579	31,205	6.23	-12.36	31,209
SAN FRANCISCO	136,837	1.61	-21.60	137,367	87,808	1.99	-41.13	89,058
SYSTEM TOTAL	1,408,512	2.29	-14.38	1,483,227	766,702	3.86	-16.37	769,653

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000					FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	CURRENCY - 3090				TOTAL	COIN - 3100			
ACTIVITY:						PAYING & RECEIVING - 3102			
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSEMENTS	NET COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
							AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	98,174	528,261	2,079,910		2,079,910	241,150	0.28	0.47	307,048
NEW YORK	143,937	1,629,564	6,265,769		6,265,769	399,680	0.53	-2.81	426,695
PHILADELPHIA	73,454	552,257	1,758,073		1,758,073	180,177	0.24	-27.51	188,776
CLEVELAND	45,312	557,095	1,575,490		1,575,490	253,071	0.18	-26.17	253,071
RICHMOND	228,521	827,928	2,766,155		2,766,155	288,690	0.19	-35.52	289,607
ATLANTA	127,650	1,179,735	2,741,324		2,741,324	189,204	0.08	-1.90	190,636
CHICAGO	109,045	666,129	2,336,133		2,336,133	278,778	0.14	-29.23	279,304
ST. LOUIS	33,339	362,215	977,998		977,998	141,259	0.26	-30.60	146,133
MINNEAPOLIS	19,461	264,570	729,371		729,371	152,066	0.34	-52.02	152,066
KANSAS CITY	41,690	451,463	1,311,701		1,311,701	172,107	0.23	-38.67	174,667
DALLAS	48,106	456,554	1,313,148		1,313,148	165,484	0.18	-49.98	165,484
SAN FRANCISCO	88,487	1,195,214	3,824,969		3,824,969	325,505	0.15	-45.64	350,046
SYSTEM TOTAL	1,049,175	8,670,985	27,680,041		27,680,041	2,767,267	0.10	-32.48	2,903,729

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	COIN - 3100				COIN - 3100				TOTAL
ACTIVITY:	VERIFYING DEPOSITS - 3105								
		UNIT PRODUCTION COST							
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON	35,852	0.18	-11.81	35,852	7,757	187,450	538,103		538,103
NEW YORK	90,890	0.31	43.47	90,527	1,334	269,314	795,870		795,870
PHILADELPHIA	23,786	0.10	-21.94	23,786	2,781	109,572	317,915		317,915
CLEVELAND	30,298	0.07	-10.38	30,298	2,318	220,745	506,428		506,428
RICHMOND	68,428	0.08	-6.18	68,711	2,562	263,755	620,636		620,636
ATLANTA	33,511	0.04	-20.98	33,882	3,769	120,271	348,758		348,758
CHICAGO	48,672	0.08	1.45	48,734	5,082	203,032	536,542		536,542
ST. LOUIS	17,216	0.07	-38.19	17,216	1,698	162,195	328,234		328,234
MINNEAPOLIS	25,988	0.17	4.93	25,988	2,713	98,548	279,315		279,315
KANSAS CITY	37,538	0.15	-25.40	37,948	1,260	191,616	405,499		405,499
DALLAS	27,990	0.07	-10.90	27,990	1,223	199,357	374,054		374,054
SAN FRANCISCO	54,532	0.09	-22.66	54,776	1,085	376,588	791,295		791,295
SYSTEM TOTAL	490,689	0.10	-9.43	499,694	35,783	2,403,443	5,842,649		5,842,649

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	TRANSFER OF ACCOUNT BALANCES - 3250				TRANSFER OF ACCOUNT BALANCES - 3250				TOTAL
ACTIVITY:	TRANSFER OF ACCOUNT BALANCES - 3252								
		UNIT PRODUCTION COST							
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON	329,430	0.30	6.27	440,485	69,016	152,646	662,147		662,147
NEW YORK	1,810,750	0.41	-26.48	1,823,616	128,973	686,073	2,638,662		2,638,662
PHILADELPHIA	279,341	0.45	-12.24	291,891	18,030	155,320	465,241		465,241
CLEVELAND	333,536	0.39	-0.55	333,536	86,242	106,657	526,435		526,435
RICHMOND	439,927	0.47	15.72	475,028	165,151	215,168	855,347		855,347
ATLANTA	505,660	0.33	-4.88	524,993	283,062	312,504	1,090,559		1,090,559
CHICAGO	1,015,440	0.51	-16.19	1,036,064	69,334	412,251	1,517,649		1,517,649
ST. LOUIS	262,794	0.35	-26.88	272,342	13,644	218,518	504,504		504,504
MINNEAPOLIS	378,185	0.77	11.79	378,185	23,066	227,839	629,090		629,090
KANSAS CITY	390,557	0.34	12.25	390,557	62,180	310,696	763,433		763,433
DALLAS	538,862	0.38	-9.64	538,862	221,852	251,431	1,012,145		1,012,145
SAN FRANCISCO	633,266	0.31	69.74	671,963	164,999	694,074	1,535,036		1,535,036
SYSTEM TOTAL	6,927,754	0.40	-8.94	7,177,527	1,169,549	3,783,177	12,150,288		12,150,288

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	AUTOMATED CLEARING HOUSE OPERATIONS - 3260				AUTOMATED CLEARING HOUSE OPERATIONS - 3260				TOTAL
ACTIVITY:	AUTOMATED CLEARING HOUSE OPERATIONS - 3262								
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
		AMOUNT	% CHANGE FROM YEAR AGO						
BOSTON	276,376	26.22	-0.76	330,709	95,991	119,492	546,192		546,192
NEW YORK	651,175	101.10	-3.61	651,578	82,906	130,249	864,733		864,733
PHILADELPHIA	206,097	33.27	-7.62	209,989	46,277	171,227	427,493		427,493
CLEVELAND	532,639	61.91	-14.16	532,639	120,961	236,328	889,928		889,928
RICHMOND	921,976	63.91	19.05	923,732	137,417	374,691	1,435,840		1,435,840
ATLANTA	811,313	30.73	-10.06	822,909	121,482	258,397	1,202,788		1,202,788
CHICAGO	950,569	47.19	-12.20	950,739	157,585	399,578	1,507,902		1,507,902
ST. LOUIS	506,076	67.08	-0.96	515,622	105,636	285,468	906,726		906,726
MINNEAPOLIS	428,125	62.01	17.21	428,125	93,271	126,038	647,434		647,434
KANSAS CITY	696,030	50.31	-12.48	697,554	132,292	246,585	1,076,431		1,076,431
DALLAS	558,761	49.61	23.81	558,761	83,579	275,845	918,185		918,185
SAN FRANCISCO	1,065,153	35.84	37.31	1,205,598	220,561	486,815	1,912,974		1,912,974
SYSTEM TOTAL	7,603,068	45.48	2.57	7,868,015	1,397,968	3,070,713	12,336,696		12,336,696

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	COMMERCIAL CHECKS - 3360				COMMERCIAL CHECKS - 3360			
ACTIVITY:	PROCESSING - 3362				ADJUSTMENTS - 3364			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	3,098,636	16.49	-0.83	3,100,162	348,330	7.35	3.28	351,356
NEW YORK	6,667,271	16.98	6.89	6,722,971	1,710,528	12.39	22.76	1,710,528
PHILADELPHIA	1,978,938	15.58	-3.39	1,984,030	292,571	7.11	0.89	292,571
CLEVELAND	2,930,375	14.08	-3.96	2,930,375	361,882	5.83	-6.10	361,882
RICHMOND	4,707,017	16.39	12.96	4,874,023	587,526	8.43	-3.00	598,839
ATLANTA	5,792,621	10.29	0.62	6,077,223	753,128	3.21	24.07	755,355
CHICAGO	6,666,058	14.86	3.70	6,668,161	1,253,725	7.38	-13.05	1,254,607
ST. LOUIS	2,118,939	16.04	-0.33	2,123,713	198,068	6.25	13.10	198,068
MINNEAPOLIS	3,492,366	17.61	16.45	3,492,366	393,119	9.85	26.50	393,119
KANSAS CITY	3,552,334	14.93	0.74	3,958,684	335,805	7.23	1.06	338,389
DALLAS	3,348,102	13.05	5.78	3,348,102	465,634	5.92	34.55	465,634
SAN FRANCISCO	3,923,884	11.38	-0.20	4,014,108	654,258	5.06	4.06	667,854
SYSTEM TOTAL	48,348,137	14.18	3.35	48,895,498	7,376,476	6.84	7.18	7,401,510

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	COMMERCIAL CHECKS - 3360				COMMERCIAL CHECKS - 3360			
ACTIVITY:	RETURN ITEMS - 3366				FINE SORT - 3367			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	312,067	139.63	-16.98	315,847	108,655	1.49	8.53	109,258
NEW YORK	776,409	160.02	33.24	789,615	633,339	5.08	43.22	633,339
PHILADELPHIA	158,406	97.48	-3.94	158,406	158,309	3.32	-1.94	158,309
CLEVELAND	271,269	109.65	-5.62	271,269	53,446	1.49	-15.12	53,446
RICHMOND	334,763	91.94	-9.61	335,055	124,193	1.53	30.36	124,283
ATLANTA	449,721	69.33	11.06	451,188	84,793	3.28	21.24	84,793
CHICAGO	464,838	89.13	-12.95	465,032	258,520	1.98	-1.10	258,738
ST. LOUIS	250,555	99.55	22.17	250,555	225,402	1.88	29.78	225,402
MINNEAPOLIS	191,522	93.74	1.59	191,522	48,087	2.43	16.24	48,087
KANSAS CITY	402,203	102.13	23.22	403,278	108,782	1.69	20.78	108,914
DALLAS	741,288	105.79	2.55	741,288	73,014	0.60	37.53	73,014
SAN FRANCISCO	616,743	89.01	5.13	732,348	273,634	2.08	19.74	274,225
SYSTEM TOTAL	4,969,778	100.41	5.19	5,105,351	2,142,974	2.01	15.53	2,144,600

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000					FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	COMMERCIAL CHECKS - 3360				TOTAL	OTHER CHECKS - 3450			
ACTIVITY:						GOVERNMENT CHECK PROCESSING - 3454			
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
							AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	105,529	1,321,495	5,311,645		5,311,645	124,604	16.99	27.37	125,109
NEW YORK	115,705	2,781,814	12,753,958		12,753,958	263,317	17.77	17.95	263,351
PHILADELPHIA	48,172	1,056,847	3,699,135		3,699,135	89,003	13.05	-24.39	89,003
CLEVELAND	43,302	1,320,976	5,011,450		5,011,450	206,542	21.18	6.13	206,542
RICHMOND	37,472	1,604,024	7,565,696		7,565,696	272,074	15.20	15.62	272,303
ATLANTA	158,329	2,066,512	9,593,360		9,593,360	402,944	20.69	17.09	421,525
CHICAGO	120,247	3,078,134	11,844,911		11,844,911	318,069	18.84	15.26	318,295
ST. LOUIS	57,607	1,257,914	4,113,251		4,113,251	172,571	20.62	24.49	172,571
MINNEAPOLIS	77,835	1,310,080	5,513,009		5,513,009	81,678	21.78	9.75	81,678
KANSAS CITY	66,502	1,515,972	5,983,911		5,983,911	104,121	14.62	3.25	104,776
DALLAS	127,756	1,507,646	6,296,238		6,296,238	147,586	17.58	24.59	147,586
SAN FRANCISCO	100,138	2,514,215	8,302,088		8,302,088	439,763	20.38	15.43	448,364
SYSTEM TOTAL	1,058,074	21,384,429	85,990,262		85,990,262	2,622,272	18.44	13.82	2,643,102

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	OTHER CHECKS - 3450				OTHER CHECKS - 3450				TOTAL
ACTIVITY:	POSTAL MONEY ORDER PROCESSING - 3454								
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
		AMOUNT	% CHANGE FROM YEAR AGO						
BOSTON	8,981			8,981	3,117	46,758	183,965	283	183,682
NEW YORK	22,978			22,978	1,633	66,787	374,749		374,749
PHILADELPHIA	6,873		-100.00	6,873	2,556	54,293	152,004	1,072	150,932
CLEVELAND	17,894		-100.00	17,894	1,512	90,841	316,789		316,789
RICHMOND	15,505		-100.00	15,635	2,297	79,640	369,874	3,805	366,069
ATLANTA	28,780		-100.00	29,143	7,378	126,024	584,070	3,023	581,047
CHICAGO	40,480		-100.00	40,493	8,383	97,337	460,708		460,708
ST. LOUIS	361,091	11.25	22.90	361,091	6,908	214,616	752,986	312,734	440,252
MINNEAPOLIS	9,723		-100.00	9,723	1,329	36,673	129,403	12,349	117,054
KANSAS CITY	9,000			9,485	2,345	45,875	162,489	13,384	149,105
DALLAS	15,042			15,042	1,839	60,223	232,610		232,610
SAN FRANCISCO	21,560			21,025	1,902	137,128	601,295		601,295
SYSTEM TOTAL	558,403	17.39	9.99	559,167	35,403	1,083,990	4,321,662	347,450	3,974,212

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	BOOK-ENTRY SECURITIES - 3520				BOOK-ENTRY SECURITIES - 3520				TOTAL
ACTIVITY:	BOOK-ENTRY SAFEKEEPING AND TRANSFER - 3521								
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
		AMOUNT	% CHANGE FROM YEAR AGO						
BOSTON	117,398	1.71		155,091	83,464	42,267	280,822		280,822
NEW YORK	1,577,451	1.28		1,577,702	14,761	305,570	1,898,033		1,898,033
PHILADELPHIA	79,546	2.47		85,438	8,606	69,232	163,276		163,276
CLEVELAND	102,230	3.23		102,230	24,464	85,056	211,750		211,750
RICHMOND	114,305	2.77		114,449	53,754	61,192	229,395		229,395
ATLANTA	112,576	2.76		112,576	48,298	57,973	218,847		218,847
CHICAGO	305,630	2.62		309,769	24,700	155,702	490,171		490,171
ST. LOUIS	66,500	2.15		71,274	10,430	56,309	138,013		138,013
MINNEAPOLIS	177,619	4.08		177,619	44,665	45,231	267,515		267,515
KANSAS CITY	75,736	3.27		80,521	9,939	51,147	141,607		141,607
DALLAS	48,999	2.34		48,999	5,213	26,431	80,643		80,643
SAN FRANCISCO	274,090	3.44		293,724	20,530	166,504	480,758		480,758
SYSTEM TOTAL	3,052,160	1.72		3,129,400	348,824	1,122,606	4,600,830		4,600,830

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	DEFINITIVE SECURITIES - 3530				DEFINITIVE SECURITIES - 3530			
ACTIVITY:	DEFINITIVE SAFEKEEPING - 3531				PURCHASE AND SALE - 3532			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	26,565	6.88		27,422	10,164	6.21		10,315
NEW YORK	284,683	43.72		287,018	113	7.93		113
PHILADELPHIA	69,295	15.16		69,295	14,971	7.22		14,971
CLEVELAND	68,881	3.63		68,881	3,407	29.63		3,407
RICHMOND	77,530	29.29		77,530	766	15.02		766
ATLANTA	62,129	2.37		62,129				
CHICAGO	152,076	13.67		152,260	45,873	8.17		45,916
ST. LOUIS	26,816	2.55		26,816				
MINNEAPOLIS	29,750	10.10		29,750	5,897	8.56		5,897
KANSAS CITY	109,531	7.16		112,686	5,705	9.19		5,705
DALLAS	53,436	7.16		53,436	1,588	75.62		1,588
SAN FRANCISCO					591	32.83		591
SYSTEM TOTAL	960,688	8.07		967,815	89,075	8.21		89,269

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000					FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	DEFINITIVE SECURITIES - 3530				TOTAL	LOANS TO DEPOSITORY INST & OTHERS - 3630			
ACTIVITY:						LOANS TO DEPOSITORY INST & OTHERS - 3631			
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSEMENTS	NET COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
							AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	9,858	33,018	88,605		88,605	169,216			170,992
NEW YORK	1,892	86,098	375,119	29,350	345,769	303,859			306,892
PHILADELPHIA	2,425	61,807	168,098		168,098	128,526			128,526
CLEVELAND	737	78,112	163,137		163,137	73,166			73,166
RICHMOND	5,992	40,833	125,121		125,121	61,876			61,881
ATLANTA	8,890	82,912	153,931		153,931	129,266			129,266
CHICAGO	5,977	111,263	315,416		315,416	290,170			300,755
ST. LOUIS	1,283	41,338	69,395		69,395	101,020			105,602
MINNEAPOLIS	5,018	18,993	59,658		59,658	91,321			91,321
KANSAS CITY	1,633	85,191	205,013		205,013	218,757			221,079
DALLAS	7,287	40,358	102,583		102,583	189,139			189,139
SAN FRANCISCO	2	38,488	38,997		38,997	256,665			256,723
SYSTEM TOTAL	50,070	706,318	1,813,473	29,350	1,784,123	1,961,101			2,049,518

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	LOANS TO DEPOSITORY INST & OTHERS - 3630				TOTAL
ACTIVITY:					
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON	30,250	71,236	280,478		280,478
NEW YORK	2,776	125,218	432,884		432,884
PHILADELPHIA	4,282	54,294	187,100		187,100
CLEVELAND	6,618	34,631	114,389		114,389
RICHMOND	16,344	27,968	106,193		106,193
ATLANTA	16,695	49,673	190,634		190,634
CHICAGO	11,032	104,203	423,990		423,990
ST. LOUIS	3,936	55,087	164,825		164,825
MINNEAPOLIS	15,052	20,243	134,616		134,616
KANSAS CITY	3,859	64,036	289,016		289,016
DALLAS	6,017	70,629	264,585		264,585
SAN FRANCISCO	5,482	82,791	385,196		385,196
SYSTEM TOTAL	121,377	763,011	2,933,906		2,933,906

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	NON-CASH COLLECTION - 3810			
ACTIVITY:	NON-CASH COLLECTION - 3814			
		UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	94,053	1.86	-4.07	96,610
NEW YORK	556,109	2.00	-18.65	557,093
PHILADELPHIA	77,405	2.58	-4.05	77,405
CLEVELAND	184,032	2.10	6.03	184,032
RICHMOND	110,730	2.37	20.30	110,064
ATLANTA	206,921	0.80	-12.95	207,655
CHICAGO	213,524	2.46	-49.26	213,727
ST. LOUIS	128,739	1.35	-28.37	128,739
MINNEAPOLIS	125,652	1.09	-9.62	125,652
KANSAS CITY	146,567	2.23	-5.34	147,205
DALLAS	121,192	1.64	22.21	121,192
SAN FRANCISCO	66,501	3.58	61.16	69,201
SYSTEM TOTAL	2,112,225	1.74	-28.45	2,119,383

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	NON-CASH COLLECTION - 3810				TOTAL
ACTIVITY:					
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON	3,099	47,143	146,860		146,860
NEW YORK	7,084	180,453	744,630		744,630
PHILADELPHIA	1,448	53,051	131,904		131,904
CLEVELAND	3,864	105,745	293,643		293,643
RICHMOND	3,654	55,313	169,831		169,831
ATLANTA	9,059	130,609	427,323		427,323
CHICAGO	5,753	81,879	301,359		301,359
ST. LOUIS	1,431	97,262	227,432		227,432
MINNEAPOLIS	6,720	41,995	174,371		174,371
KANSAS CITY	1,914	115,685	264,804		264,804
DALLAS	8,719	83,539	213,450		213,450
SAN FRANCISCO	7,263	54,510	130,976		130,976
SYSTEM TOTAL	60,092	1,087,188	3,226,583		3,226,583

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	PUBLIC PROGRAMS - 3900			
ACTIVITY:	PUBLIC PROGRAMS - 3904			
		UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	398,474			400,088
NEW YORK	894,199			894,199
PHILADELPHIA	391,090			391,090
CLEVELAND	293,467			293,467
RICHMOND	523,003			523,203
ATLANTA	416,774			416,774
CHICAGO	611,974			612,534
ST. LOUIS	668,127			668,127
MINNEAPOLIS	332,827			332,827
KANSAS CITY	439,269			439,532
DALLAS	390,304			390,304
SAN FRANCISCO	698,941			700,019
SYSTEM TOTAL	6,050,429			6,062,944

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000					FINANCIAL INST & THE PUBLIC - 3000			
SERVICE:	PUBLIC PROGRAMS - 3900				TOTAL	OTHER - 3980			
ACTIVITY:						SERVICES TO OTHER CENTRAL BANKS - 3984			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE- MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	9,239	100,884	510,121		510,121				
NEW YORK	2,433	256,123	1,152,755		1,152,755	1,927,066			1,927,779
PHILADELPHIA	6,765	102,046	499,921		499,921				
CLEVELAND	2,072	122,502	418,021		418,021				
RICHMOND	4,933	138,294	658,430		658,430				
ATLANTA	7,656	149,533	573,963		573,963	44,937			44,937
CHICAGO	11,099	202,607	827,040		827,040				
ST. LOUIS	5,864	189,036	863,027		863,027				
MINNEAPOLIS	5,994	72,313	410,724		410,724				
KANSAS CITY	2,521	155,248	597,301		597,301				
DALLAS	4,900	189,271	544,475		544,475	6,161			6,161
SAN FRANCISCO	2,931	264,685	968,435		968,435	3,807			3,807
SYSTEM TOTAL	66,807	1,894,482	8,024,233		8,024,233	1,981,971			1,982,684

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000				FINANCIAL INST & THE PUBLIC - 3000				
SERVICE:	OTHER - 3980				OTHER - 3980				TOTAL
ACTIVITY:	SERVICES RENDERED OTHERS - 3988								
		UNIT PRODUCTION COST							
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE- MENTS	NET COST
BOSTON	217,980			221,125	5,297	76,349	302,771		302,771
NEW YORK	427,785			427,789	6,528	641,179	3,003,275	183,961	2,819,314
PHILADELPHIA	45,528			45,528	2,162	50,456	98,146		98,146
CLEVELAND	246,199			246,199	1,613	67,145	314,957		314,957
RICHMOND	170,193			170,206	991	592,629	763,826		763,826
ATLANTA	130,690			130,690	2,906	97,602	276,135		276,135
CHICAGO	80,351			80,412	1,307	21,665	103,424		103,424
ST. LOUIS	56,053			56,053	920	19,998	76,971		76,971
MINNEAPOLIS	17,208			17,208	287	3,082	20,577		20,577
KANSAS CITY	112,362			112,765	529	21,123	134,397		134,397
DALLAS	45,613			45,613	718	14,935	67,427		67,427
SAN FRANCISCO	10,304			10,304	69	129,888	138,984		138,984
SYSTEM TOTAL	1,560,189			1,563,872	23,367	1,735,967	5,300,890	183,961	5,116,929

SERVICE LINE:	FINANCIAL INST & THE PUBLIC - 3000		
SERVICE:	TOTAL		
ACTIVITY:			
FEDERAL RESERVE DISTRICT	TOTAL COST	REIMBURSE-MENTS	NET COST
BOSTON	11,024,812	283	11,024,529
NEW YORK	31,300,537	213,311	31,087,226
PHILADELPHIA	8,357,177	1,872	8,355,305
CLEVELAND	10,720,499		10,720,499
RICHMOND	15,667,538	3,809	15,663,729
ATLANTA	17,360,745	3,023	17,357,722
CHICAGO	20,808,759		20,808,759
ST. LOUIS	9,179,790	312,734	8,867,056
MINNEAPOLIS	9,424,030	12,349	9,411,681
KANSAS CITY	11,409,850	13,384	11,396,466
DALLAS	11,904,891		11,904,891
SAN FRANCISCO	20,735,520		20,735,520
SYSTEM TOTAL	177,894,144	560,761	177,333,383

SERVICE LINE:	SUPERVISION & REGULATION - 4000				SUPERVISION & REGULATION - 4000			
SERVICE:	SUPERVISION OF DIST FINANCIAL INST - 4300				SUPERVISION OF DIST FINANCIAL INST - 4300			
ACTIVITY:	CONSUMER AFFAIRS EXAMINATIONS - 4301				COMMERCIAL BANK EXAMINATIONS - 4303			
		UNIT PRODUCTION COST				UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	17,318	8,659.00	35.47	17,318	146,796		-100.00	146,796
NEW YORK	234,596	26,066.22	13.74	234,596	919,760	25.48	17.02	919,760
PHILADELPHIA	84,983	21,245.75	30.56	84,983	189,576	5,575.76	11,991.27	189,576
CLEVELAND	102,511	7,885.46	-36.60	102,511	379,318	491.98	-28.37	379,318
RICHMOND	133,466	5,802.87	13.07	133,466	493,694	225.12	-84.02	493,694
ATLANTA	84,563	5,285.19	13.52	84,563	481,590	1,352.78	26.86	481,590
CHICAGO	229,937	8,516.19	20.04	230,298	769,320	77.59	-83.58	770,169
ST. LOUIS	60,332	5,027.67	-41.93	60,332	233,438	1,032.91	116.53	233,438
MINNEAPOLIS	94,740	4,737.00	-1.23	94,740	270,733	721.95	-28.40	270,733
KANSAS CITY	94,426	4,496.48	46.88	94,426	451,171	383.08	-16.27	451,171
DALLAS	76,428	6,369.00	4.80	76,428	359,322	1,466.62	-10.03	359,322
SAN FRANCISCO	197,758	21,973.11	10.84	197,758	773,077	134.05	-79.70	775,599
SYSTEM TOTAL	1,411,058	8,399.15	12.19	1,411,419	5,467,799	95.67	-1.28	5,471,170

SERVICE LINE:	SUPERVISION & REGULATION - 4000				SUPERVISION & REGULATION - 4000			
SERVICE:	SUPERVISION OF DIST FINANCIAL INST - 4300				SUPERVISION OF DIST FINANCIAL INST - 4300			
ACTIVITY:	OTHER RESERVE BANK EXAMINATIONS - 4304				INTERNATIONAL BANKING ORG EXAMINATIONS - 4305			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	84,701	16,940.20	-19.44	84,701	24,206	8,068.67	-39.29	24,206
NEW YORK	578,222	13,447.02	-6.51	578,222	454,135	41,285.00	-27.71	454,135
PHILADELPHIA	128,659	42,886.33	307.82	128,659	169,832	169,832.00	19.67	169,832
CLEVELAND	130,360	13,036.00	54.31	130,360	4,860	810.00	-72.70	4,860
RICHMOND	101,907	5,661.50	43.83	101,907	1,809	603.00	7.77	1,809
ATLANTA	83,522	5,965.86	4.93	83,522	71,705	8,963.13	86.41	71,705
CHICAGO	279,272	6,206.04	50.25	279,414	150,868	75,434.00	585.00	151,094
ST. LOUIS	100,262	5,013.10	-47.24	100,262	953		-100.00	953
MINNEAPOLIS	75,543	6,295.25	-0.55	75,543	5,336			5,336
KANSAS CITY	64,439	4,956.85	83.26	64,439				
DALLAS	41,992	8,398.40	36.10	41,992	53,370	6,671.25	-26.43	53,370
SAN FRANCISCO	172,228	10,764.25	-2.56	172,228	211,777	16,290.54	190.86	218,382
SYSTEM TOTAL	1,831,107	8,976.01	19.70	1,831,249	1,128,851	20,524.56	42.37	1,135,682

SERVICE LINE:	SUPERVISION & REGULATION - 4000				SUPERVISION & REGULATION - 4000			
SERVICE:	SUPERVISION OF DIST FINANCIAL INST - 4300				SUPERVISION OF DIST FINANCIAL INST - 4300			
ACTIVITY:	BANK HOLDING CO. INSPECTIONS AND VISITS - 4306				SUPERVISING DIST FINANCIAL INSTITUTIONS - 4308			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	135,945	41.38	-3.07	135,945	176,392			177,190
NEW YORK	307,901	203.26	404.98	307,901	225,496			225,496
PHILADELPHIA	142,237	5,079.89	393.44	142,237	97,864			97,864
CLEVELAND	89,852	547.88	-73.23	89,852	68,864			68,864
RICHMOND	125,257	125.51	-9.51	125,257	7,116			7,116
ATLANTA	211,219	204.47	-75.03	211,219	29,422			29,422
CHICAGO	392,019	213.95	132.01	393,403	296,799			282,530
ST. LOUIS	136,613	101.67	2.04	136,613	67,807			67,807
MINNEAPOLIS	149,711	3.70	-99.80	149,711	96,334			96,334
KANSAS CITY	438,763	834.11	57.07	438,763	249,909			249,909
DALLAS	250,104	164.76	6.19	250,104	106,852			106,852
SAN FRANCISCO	232,118	61.10	57.01	232,116	37,491			37,491
SYSTEM TOTAL	2,612,519	47.10	-56.90	2,613,103	1,380,384			1,380,609

SERVICE LINE:	SUPERVISION & REGULATION - 4000					SUPERVISION & REGULATION - 4000			
SERVICE:	SUPERVISION OF DIST FINANCIAL INST - 4300				TOTAL	ADMIN OF LAWS & REGS RELATED TO BANKING - 4600			
ACTIVITY:						PROC BANK & INTERN'L BANKING ORG APPLI - 4601			
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSEMENTS	NET COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
							AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	73,837	198,380	848,381		848,381	9,988	1,109.78	-3.18	9,988
NEW YORK	28,519	796,015	3,584,648		3,584,648	118,713	1,918.73	-5.33	118,713
PHILADELPHIA	48,005	212,161	1,004,321		1,004,321	24,053	3,006.63	128.66	24,053
CLEVELAND	23,027	260,073	1,030,865		1,030,865	13,453	2,242.17	-79.13	13,453
RICHMOND	24,234	262,237	1,149,718		1,149,718	22,832	815.43	-38.60	22,832
ATLANTA	82,825	316,900	1,361,746		1,361,746	15,136	5,045.33	57.38	15,136
CHICAGO	94,850	505,952	2,727,718		2,727,718	42,205	794.32	2.18	42,278
ST. LOUIS	23,250	205,625	828,280		828,280	5,793		-100.00	5,793
MINNEAPOLIS	34,309	195,095	921,881		921,881	8,957	308.86	493.97	8,957
KANSAS CITY	24,786	411,002	1,734,476		1,734,476	18,067	9,033.50	374.33	18,067
DALLAS	99,072	269,865	1,257,085		1,257,085	11,489	1,276.56	-33.99	11,489
SAN FRANCISCO	22,779	510,505	2,166,860		2,166,860	44,077	4,897.44	111.56	44,077
SYSTEM TOTAL	579,497	4,148,770	18,575,779		18,575,779	334,763	1,535.61	13.51	334,836

SERVICE LINE:	SUPERVISION & REGULATION - 4000				SUPERVISION & REGULATION - 4000			
SERVICE:	ADMIN OF LAWS & REGS RELATED TO BANKING - 4600				ADMIN OF LAWS & REGS RELATED TO BANKING - 4600			
ACTIVITY:	PROCESSING HOLDING COMPANY APPLICATIONS - 4602				COLL & PROC CONDITION & OTHER STAT RPTS - 4604			
FEDERAL RESERVE DISTRICT	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST	PRODUCTION COST	UNIT PRODUCTION COST		TOTAL ACTIVITY COST
		AMOUNT	% CHANGE FROM YEAR AGO			AMOUNT	% CHANGE FROM YEAR AGO	
BOSTON	100,454	4,566.09	23.30	100,454	66,850			69,924
NEW YORK	169,438	1,711.49	-29.28	169,438	485,596			485,596
PHILADELPHIA	48,069	4,806.90	71.89	48,069	40,687			40,687
CLEVELAND	110,238	5,511.90	-35.15	110,238	88,285			88,285
RICHMOND	87,081	1,777.16	35.51	87,081	96,305			96,305
ATLANTA	114,763	2,013.39	7.96	114,763	73,949			73,949
CHICAGO	301,130	2,573.76	51.00	301,604	203,162			203,589
ST. LOUIS	134,089	3,192.60	52.53	134,089	31,572			31,572
MINNEAPOLIS	130,124	4,066.38	109.88	130,124	60,738			60,738
KANSAS CITY	176,723	2,295.10	-11.26	176,723	127,493			127,493
DALLAS	108,627	2,311.21	130.43	108,627	133,359			133,359
SAN FRANCISCO	95,295	2,324.27	100.59	95,295	203,135			203,135
SYSTEM TOTAL	1,576,031	2,571.01	32.64	1,576,505	1,611,131			1,614,632

SERVICE LINE:	SUPERVISION & REGULATION - 4000				SUPERVISION & REGULATION - 4000			
SERVICE:	ADMIN OF LAWS & REGS RELATED TO BANKING - 4600				ADMIN OF LAWS & REGS RELATED TO BANKING - 4600			
ACTIVITY:	ADMIN. & MONITORING OF REGULATIONS - 4606				MONITORING RESERVE ACCOUNTS - 4608			
		UNIT PRODUCTION COST				UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	120,092			128,092	204,099	22.55	75.00	234,038
NEW YORK	333,868			333,868	606,985	50.83	12.72	617,386
PHILADELPHIA	110,027			110,027	237,297	42.61	15.86	243,189
CLEVELAND	44,487			44,487	179,205	20.06	12.68	179,205
RICHMOND	56,869			56,869	328,303	31.68	36.65	366,627
ATLANTA	160,364			160,364	409,219	17.55	34.05	409,592
CHICAGO	226,572			226,056	723,823	22.92	37.01	726,485
ST. LOUIS	81,520			81,520	226,221	14.31	95.57	245,318
MINNEAPOLIS	52,136			52,136	360,926	34.11	81.04	360,926
KANSAS CITY	134,267			134,391	183,295	8.16	-7.76	183,673
DALLAS	152,438			152,438	457,599	17.05	26.13	457,599
SAN FRANCISCO	223,225			224,253	651,609	39.95	22.31	664,498
SYSTEM TOTAL	1,703,865			1,705,301	4,570,381	23.71	30.70	4,688,496

SERVICE LINE:	SUPERVISION & REGULATION - 4000					SUPERVISION & REGULATION - 4000			
SERVICE:	ADMIN OF LAWS & REGS RELATED TO BANKING - 4600 TOTAL					BANKING & FIN MARKET STRUCTURE STUDIES - 4900			
ACTIVITY:						MKT STRUCTURE & SUP & REG POLICY STUDIES - 4906			
							UNIT PRODUCTION COST		
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSE-MENTS	NET COST	PRODUCTION COST	AMOUNT	% CHANGE FROM YEAR AGO	TOTAL ACTIVITY COST
BOSTON	264,760	206,040	1,013,300		1,013,300	23,294			23,294
NEW YORK	226,365	702,102	2,573,420		2,573,420	397,210			397,210
PHILADELPHIA	120,177	174,984	761,186		761,186	24,200			24,200
CLEVELAND	144,047	209,662	789,777		789,777	16,359			16,359
RICHMOND	226,139	227,260	1,083,117		1,083,117	35,330			35,330
ATLANTA	210,322	279,618	1,263,704		1,263,704	165,092			165,092
CHICAGO	217,301	505,814	2,303,927	2,463	2,301,464	168,054			168,229
ST. LOUIS	85,615	185,597	769,504		769,504	7,820			7,820
MINNEAPOLIS	163,952	184,293	961,126		961,126	82,017			82,017
KANSAS CITY	72,348	222,999	935,694		935,694	114,713			114,713
DALLAS	130,082	350,765	1,384,379		1,384,379	70,813			70,813
SAN FRANCISCO	399,450	430,735	2,069,443		2,069,443	73,320			73,320
SYSTEM TOTAL	2,260,962	3,607,893	15,868,625	2,463	15,866,162	1,179,870			1,180,045

SERVICE LINE:	SUPERVISION & REGULATION - 4000					SUPERVISION & REGULATION - 4000		
SERVICE:	BANKING & FIN MARKET STRUCTURE STUDIES - 4900 TOTAL					TOTAL		
ACTIVITY:								
FEDERAL RESERVE DISTRICT	SYSTEM PROJECTS	OVERHEAD	TOTAL COST	REIMBURSEMENTS	NET COST	TOTAL COST	REIMBURSEMENTS	NET COST
BOSTON	2,900	5,055	32,049		32,049	1,893,690		1,893,690
NEW YORK	8,170	136,173	537,561		537,561	6,655,637		6,655,637
PHILADELPHIA	2,196	10,898	37,334		37,334	1,802,841		1,802,841
CLEVELAND	545	6,266	23,170		23,170	1,843,812		1,843,812
RICHMOND	985	9,429	45,788		45,788	2,278,579		2,278,579
ATLANTA	14,176	49,007	229,075		229,075	2,854,565		2,854,565
CHICAGO	7,463	40,330	216,022		216,022	5,247,667	2,463	5,245,204
ST. LOUIS	167	2,808	10,795		10,795	1,608,579		1,608,579
MINNEAPOLIS	4,101	19,283	106,201		106,201	1,989,128		1,989,128
KANSAS CITY	2,170	25,077	141,960		141,960	2,812,130		2,812,130
DALLAS	7,664	22,048	100,525		100,525	2,701,909		2,701,909
SAN FRANCISCO	1,021	15,979	90,320		90,320	4,326,623		4,326,623
SYSTEM TOTAL	51,558	343,153	1,570,756		1,570,756	36,015,160	2,463	36,012,697

SUMMARY REPORT

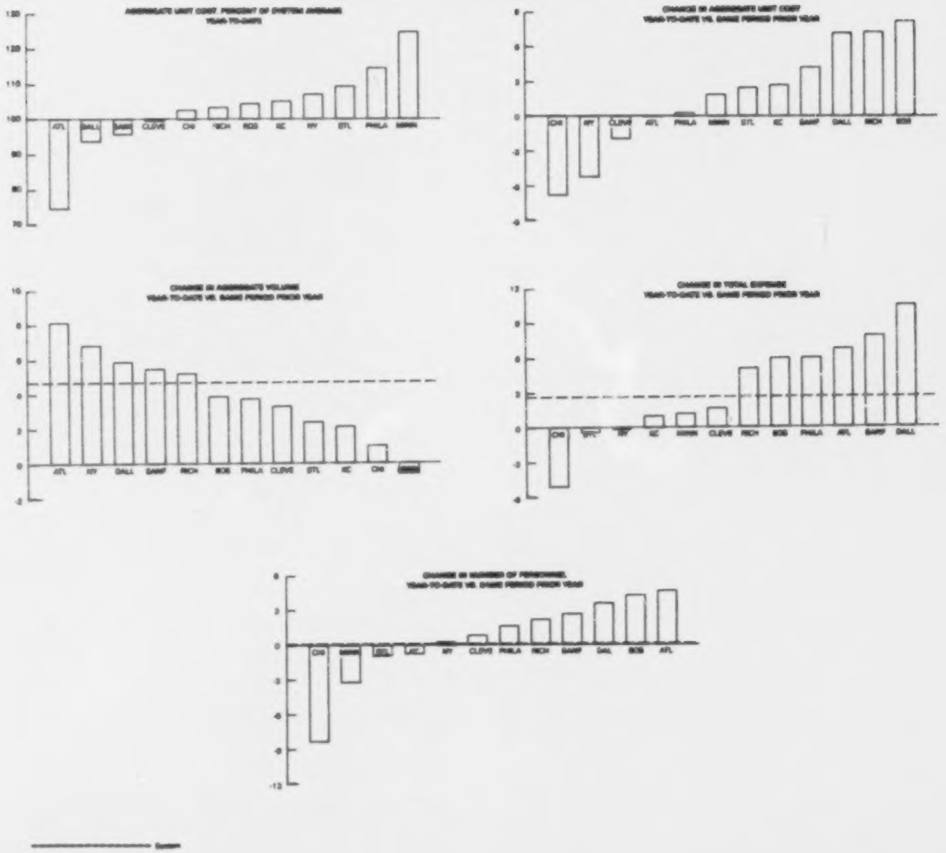
PERFORMANCE MEASURES
FIRST QUARTER, 1985

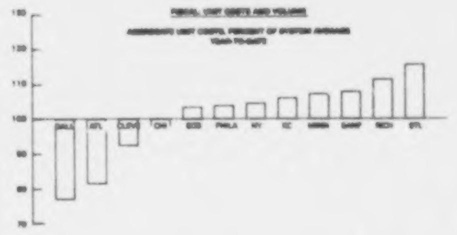
KEY QUALITY MEASURES

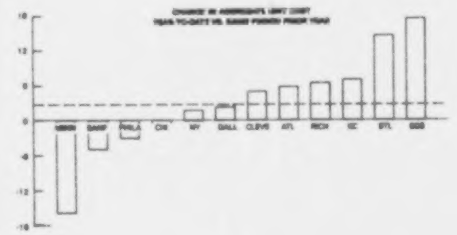
FEDERAL RESERVE DISTRICT	PRIOR - YEARS		YEAR - TO - DATE			RECENT QUARTERS				
	1983	1984		1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
QUALITY MEASURE:	% UP-TIME LAST 2 HOURS OF OPERATIONS							TRANSFER OF ACCOUNT BALANCES - 3250		
BOSTON		99.44		100.00	1	99.80	98.27	100.00	99.68	100.00
NEW YORK		97.89		98.32	12	97.84	98.63	99.26	95.74	98.32
PHILADELPHIA		99.30		99.80	6	98.88	99.06	100.00	100.00	99.80
CLEVELAND		98.58		98.66	11	99.72	97.33	98.80	98.51	98.66
RICHMOND		99.35		99.69	7	97.83	99.57	100.00	100.00	99.69
ATLANTA		100.00		100.00	2	100.00	100.00	100.00	100.00	100.00
CHICAGO		100.00		100.00	3	100.00	100.00	100.00	100.00	100.00
ST. LOUIS		98.05		98.90	10	98.82	98.82	97.09	97.87	98.90
MINNEAPOLIS		99.48		99.60	8	99.74	99.73	99.68	98.78	99.60
KANSAS CITY		99.86		100.00	4	100.00	100.00	100.00	99.82	100.00
DALLAS		99.58		100.00	5	100.00	99.28	99.30	99.74	100.00
SAN FRANCISCO		98.40		99.45	9	98.74	98.83	99.33	96.72	99.45
SYSTEM		99.17		99.54		99.25	99.13	99.46	98.84	99.54
SYSTEM TARGET		98.50		98.50		98.50	98.50	98.50	98.50	98.50
NBR ATTAIN TARGET		9		11		9	10	11	9	11
QUALITY MEASURE:	PERCENT SUSPENSE ENTRIES OVER ONE MONTH OLD							COMMERCIAL CHECKS - 3360		
BOSTON	.09	1.13		.96	4	.09	.15	1.44	1.92	.96
NEW YORK	10.64	34.07		44.23	12	35.47	23.00	39.90	37.20	44.23
PHILADELPHIA					1					
CLEVELAND	1°.58	19.30		16.57	8	19.74	20.84	20.69	16.04	16.57
RICHMOND	22.63	21.80		13.03	7	14.39	19.04	25.73	26.13	13.03
ATLANTA	.76	4.59		1.12	5	2.30	7.67	5.58	3.10	1.12
CHICAGO	41.90	14.27		24.97	11	12.91	8.13	16.86	15.69	24.97
ST. LOUIS	17.96	5.34		.79	3	4.87	13.17	1.50	.99	.79
MINNEAPOLIS	17.25	18.09		20.59	10	14.44	18.31	16.45	22.07	20.59
KANSAS CITY	21.97	30.91		18.19	9	43.20	40.53	25.89	19.09	18.19
DALLAS	2.57	1.60		6.84	6	3.63	1.06	1.12	.41	6.84
SAN FRANCISCO	.95	.27		.17	2	.53	.25	.29	.08	.17
SYSTEM	18.07	17.09		17.81		18.76	13.30	19.28	16.68	17.81
SYSTEM TARGET		10.00		10.00		10.00	10.00	10.00	10.00	10.00
NBR ATTAIN TARGET		6		6		6	6	6	6	6
QUALITY MEASURE:	AV # DAYS TO ELIMINATE BACKLOG							COMMERCIAL CHECKS - 3360		
BOSTON	2.42	3.27		4.21	11	2.07	2.56	3.51	4.67	4.21
NEW YORK	2.93	4.77		5.29	12	4.38	4.75	5.09	4.89	5.29
PHILADELPHIA	1.71	2.41		2.11	9	3.00	2.06	2.11	1.64	2.11
CLEVELAND	1.19	1.10		1.60	7	1.04	.83	1.06	1.43	1.60
RICHMOND	1.36	1.16		1.26	5	1.28	1.12	1.16	1.09	1.26
ATLANTA	.34	.78		.96	3	.45	.75	1.10	.83	.96
CHICAGO	.85	1.32		1.48	6	1.39	1.29	1.24	1.36	1.48
ST. LOUIS	.56	.41		.47	1	.19	.20	.60	.63	.47
MINNEAPOLIS	1.42	1.56		1.21	4	1.23	1.84	1.84	1.00	1.21
KANSAS CITY	.60	.81		.86	2	1.00	.72	.85	.66	.86
DALLAS	.66	.61		1.68	8	.58	.64	.65	.58	1.68
SAN FRANCISCO	2.29	2.96		2.68	10	2.62	2.59	3.42	3.20	2.68
SYSTEM	1.30	1.83		2.07		1.66	1.70	1.97	1.89	2.07
SYSTEM TARGET		5.00		5.00		5.00	5.00	5.00	5.00	5.00
NBR ATTAIN TARGET		12		11		12	12	11	12	11
QUALITY MEASURE:	ADJUSTMENT CASES/100,000 CHECKS PROC							COMMERCIAL CHECKS - 3360		
BOSTON	13.82	14.60		16.39	1	14.40	14.08	15.25	14.61	16.39
NEW YORK	28.13	28.84		26.93	9	31.95	29.90	27.20	26.35	26.93
PHILADELPHIA	21.74	24.38		24.12	7	24.92	26.15	23.80	22.78	24.12
CLEVELAND	22.88	25.81		27.19	10	26.02	24.56	25.78	26.87	27.19
RICHMOND	17.15	18.53		20.32	5	19.07	17.78	18.41	18.07	20.32
ATLANTA	43.19	41.80		41.46	12	44.20	41.01	41.29	40.80	41.46
CHICAGO	28.26	32.95		33.31	11	35.05	30.48	35.15	31.33	33.31
ST. LOUIS	15.95	16.38		16.58	2	19.88	15.96	15.36	14.40	16.58
MINNEAPOLIS	14.89	16.83		18.22	4	16.67	16.32	16.79	17.58	18.22
KANSAS CITY	15.21	17.13		17.34	3	17.24	16.69	17.64	16.97	17.34
DALLAS	34.96	36.77		26.69	8	36.16	38.56	38.72	33.88	26.69
SAN FRANCISCO	19.70	20.29		20.39	6	20.93	19.65	20.24	20.37	20.39
SYSTEM	24.75	26.29		25.88		27.51	25.87	26.41	25.44	25.88
SYSTEM TARGET		25.00		25.00		25.00	25.00	25.00	25.00	25.00
NBR ATTAIN TARGET		7		7		7	7	7	7	7
QUALITY MEASURE:	% INCORRECT DEFINITIVE TRANSACTIONS							DEFINITIVE SECURITIES - 3530		
BOSTON		.13			1			.48	.05	
NEW YORK	.16	.18			2	.26	.06	.19	.20	
PHILADELPHIA	.23			.59	12	.21				.59
CLEVELAND	.26	.18		.20	11	.18	.24	.13	.18	.20
RICHMOND	.37	.10			3	.26			.10	
ATLANTA		.01			4			.05		
CHICAGO	.12	.12		.03	9	.32	.04	.04		.03
ST. LOUIS	.13				5					
MINNEAPOLIS	.58	.54			6	.06	1.30			
KANSAS CITY	.11	.02		.06	10			.03	.04	.06
DALLAS	.05	.03			7		.12			
SAN FRANCISCO					8					
SYSTEM	.14	.01		.06		.14		.08	.04	.06
SYSTEM TARGET		1.00		1.00		1.00	1.00	1.00	1.00	1.00
NBR ATTAIN TARGET		12		12		12	11	12	12	12
QUALITY MEASURE:	% SECURITIES TRANSFER SYS OPER-TIME							BOOK-ENTRY SECURITIES - 3520		
BOSTON	97.87	98.94		98.89	7	99.19	98.34	99.12	99.14	98.89
NEW YORK	97.27	97.94		99.11	4	96.96	98.29	98.19	98.67	99.11
PHILADELPHIA	96.96	95.50		96.72	12	94.73	96.34	96.99	99.09	96.72
CLEVELAND	96.00	96.04		98.80	11	98.03	97.83	99.32	98.92	98.80
RICHMOND	98.44	98.41		99.36	3	95.18	99.28	99.76	99.49	99.36
ATLANTA	100.15	94.58		98.83	9	98.56	96.80	94.39	88.65	98.83
CHICAGO	97.35	99.36		100.00	1	97.36	100.00	100.00	100.00	100.00
ST. LOUIS	96.39	98.57		98.87	8	98.53	98.49	98.93	98.49	98.87
MINNEAPOLIS	95.53	97.36		98.96	6	98.11	97.43	98.74	95.28	98.96
KANSAS CITY	98.85	98.64		99.64	2	97.54	99.25	99.24	98.53	99.64
DALLAS	97.85	98.81		98.81	10	99.43	98.72	98.38	98.80	98.81
SAN FRANCISCO	98.30	98.76		99.11	5	97.96	98.73	99.07	98.85	99.11
SYSTEM	98.16	97.48		98.93		98.18	98.20	97.69	95.91	98.93
SYSTEM TARGET		99.00		99.00		99.00	99.00	99.00	99.00	99.00
NBR ATTAIN TARGET		1		12		2	3	6	3	12

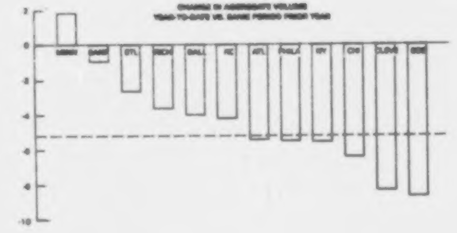
FEDERAL RESERVE DISTRICT	PRIOR - YEARS		YEAR - TO - DATE			RECENT QUARTERS				
	1983	1984		1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
QUALITY MEASURE:	% INCORRECT OFF-LINE B-E TRANSACTIONS						BOOK-ENTRY SECURITIES - 3520			
BOSTON	.01				1					
NEW YORK	.12	.20		.20	12	.16	.11	.17	.39	.20
PHILADELPHIA	.35	.40		.17	10	.03	.49	.13	.48	.17
CLEVELAND		.09			2		.26	.08	.03	
RICHMOND	.07	.03		.02	6	.06		.03	.03	.02
ATLANTA	.01	.02		.18	11	.10				.18
CHICAGO	.06	.02		.07	8	.06	.02	.01		.07
ST. LOUIS	.03	.09		.02	7	.16	.21			.02
MINNEAPOLIS	.16				3					
KANSAS CITY	.03	.07		.14	9	.08	.04	.10	.08	.14
DALLAS	.01				4					
SAN FRANCISCO					5					
SYSTEM	.06	.08		.11		.09	.07	.06	.10	.11
SYSTEM TARGET		1.00		1.00		1.00	1.00	1.00	1.00	1.00
BKS ATTAIN TARGET		12		12		12	12	12	12	12
QUALITY MEASURE:	% INCORRECT COLLECTION TRANSACTIONS						NON-CASH COLLECTION - 3810			
BOSTON	.16	.01			1		.03			
NEW YORK					2					
PHILADELPHIA	.23	.33		.38	10	.45	.24	.34	.33	.30
CLEVELAND	.35	.33		.47	11	.33	.29	.41	.30	.47
RICHMOND	.02	.01		.01	6		.01	.01	.03	.01
ATLANTA	.02	.02		.01	7	.04	.02	.02	.01	.01
CHICAGO	.05	.02			3	.04				
ST. LOUIS	.02	.01		.07	8	.04	.01			.07
MINNEAPOLIS	.15	.21		1.10	12	.96	.40	.05		1.10
KANSAS CITY	.12	.18		.20	9	.15	.20	.22	.15	.20
DALLAS	.01				4					
SAN FRANCISCO	.04				5		.01			
SYSTEM	.07	.07		.13		.08	.07	.06	.05	.13
SYSTEM TARGET		1.00		1.00		1.00	1.00	1.00	1.00	1.00
BKS ATTAIN TARGET		12		11		12	12	12	12	11
QUALITY MEASURE:	AS OF ADJ BY RES BKS/1,000 ENTRIES PROC						GENERAL BOOKS & BUDGET & EXPENSE CONTROL - 0330			
BOSTON	.35	.32		.28	1	.31	.31	.33	.31	.29
NEW YORK	.66	.60		.38	3	.64	.61	.37	.63	.30
PHILADELPHIA	1.25	.72		.48	6	.96	.64	.59	.70	.48
CLEVELAND	1.52	1.27		1.22	11	1.35	1.11	1.37	1.25	1.22
RICHMOND	.48	.48		.35	5	.99	.25	.31	.35	.35
ATLANTA	.52	.47		.63	9	.46	.52	.36	.55	.63
CHICAGO	.35	.59		1.28	12	.39	.38	.55	1.29	1.28
ST. LOUIS	.77	.44		.48	7	.50	.45	.36	.44	.48
MINNEAPOLIS	.64	.65		.71	10	.67	.73	.54	.82	.71
KANSAS CITY	.45	.61		.50	8	.52	.75	.57	.62	.50
DALLAS	.48	.33		.34	4	.35	.29	.33	.34	.34
SAN FRANCISCO	.64	.26		.29	2	.20	.26	.25	.28	.29
SYSTEM	.61	.51		.52		.54	.47	.46	.50	.52
SYSTEM TARGET		.75		.75		.75	.75	.75	.75	.75
BKS ATTAIN TARGET		11		10		9	11	11	9	10
QUALITY MEASURE:	AV # CONTROL OVERDRAFTS/100 ACCTS						GENERAL BOOKS & BUDGET & EXPENSE CONTROL - 0330			
BOSTON	.32	.39		.28	6	.27	.46	.49	.34	.28
NEW YORK	.26	.33		.48	12	.44	.41	.36	.13	.48
PHILADELPHIA	.98	.66		.47	11	.69	.63	.50	.82	.47
CLEVELAND	.51	.44		.44	10	.34	.43	.54	.43	.44
RICHMOND	.18	.24		.08	2	.54	.15	.13	.18	.08
ATLANTA	.29	.30		.34	8	.39	.45	.19	.18	.34
CHICAGO	.32	.27		.17	4	.27	.21	.33	.25	.17
ST. LOUIS	.26	.24		.19	5	.23	.23	.21	.27	.19
MINNEAPOLIS	.35	.33		.13	3	.31	.42	.31	.28	.13
KANSAS CITY	.02	.05		.06	1	.04	.04	.04	.07	.06
DALLAS	.33	.29		.41	9	.30	.19	.28	.31	.41
SAN FRANCISCO	.37	.26		.26	7	.23	.27	.24	.28	.26
SYSTEM	.30	.27		.25		.31	.27	.27	.25	.25
SYSTEM TARGET		.50		.50		.50	.50	.50	.50	.50
BKS ATTAIN TARGET		11		12		10	11	11	11	12
QUALITY MEASURE:	# BILL ADJ REQ BY ERRORS/1,000 ENTRIES PROC						GENERAL BOOKS & BUDGET & EXPENSE CONTROL - 0330			
BOSTON	.21	.15		.02	2	.44	.02	.02	.12	.02
NEW YORK	.09	.07		.14	9	.05	.02	.02	.19	.14
PHILADELPHIA	.04	.03		.02	3	.02	.02	.03	.05	.02
CLEVELAND	.30	.21		.10	7	.38	.19	.16	.12	.10
RICHMOND	.26	.37		.36	12	.42	.39	.24	.45	.36
ATLANTA	.79	1.19		.17	10	.85	1.56	1.14	1.15	.17
CHICAGO	1.43	.94		.13	8	.77	.64	.48	.28	.13
ST. LOUIS	.09	.04		.01	1	.05	.04	.03	.04	.01
MINNEAPOLIS	.24	.05		.02	4	.10	.05	.01	.06	.02
KANSAS CITY	.06	.08		.04	5	.08	.13	.03	.06	.04
DALLAS	.38	.10		.04	6	.10	.15	.07	.10	.04
SAN FRANCISCO	.32	.20		.18	11	.19	.11	.23	.29	.18
SYSTEM	.41	.30		.12		.33	.34	.25	.29	.12
SYSTEM TARGET		.75		.75		.75	.75	.75	.75	.75
BKS ATTAIN TARGET		11		12		10	11	11	11	12

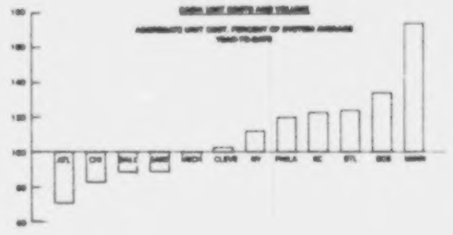
BANKWIDE UNIT COSTS, VOLUME, AND EMPLOYMENT

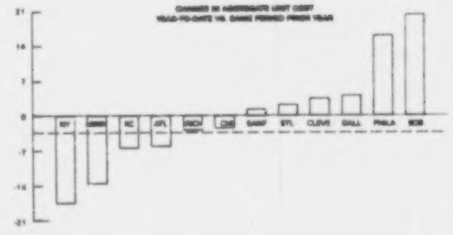


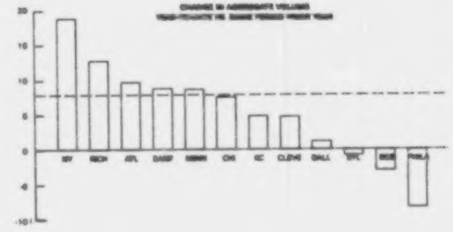

FISCAL UNIT COSTS AND VOLUME
AGGREGATE UNIT COSTS, PERCENT OF SYSTEM AVERAGE
YEAR-TO-DATE
130
120
110
100
90
80
70
DALL
ATL
CLEVE
CHI
BOS
PHILA
NY
KC
MINN
SANF
RICH
STL


CHANGE IN AGGREGATE UNIT COST
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
18
12
6
0
-6
-12
-18
MINN
SANF
PHILA
CHI
NY
DALL
CLEVE
ATL
RICH
KC
STL
BOS

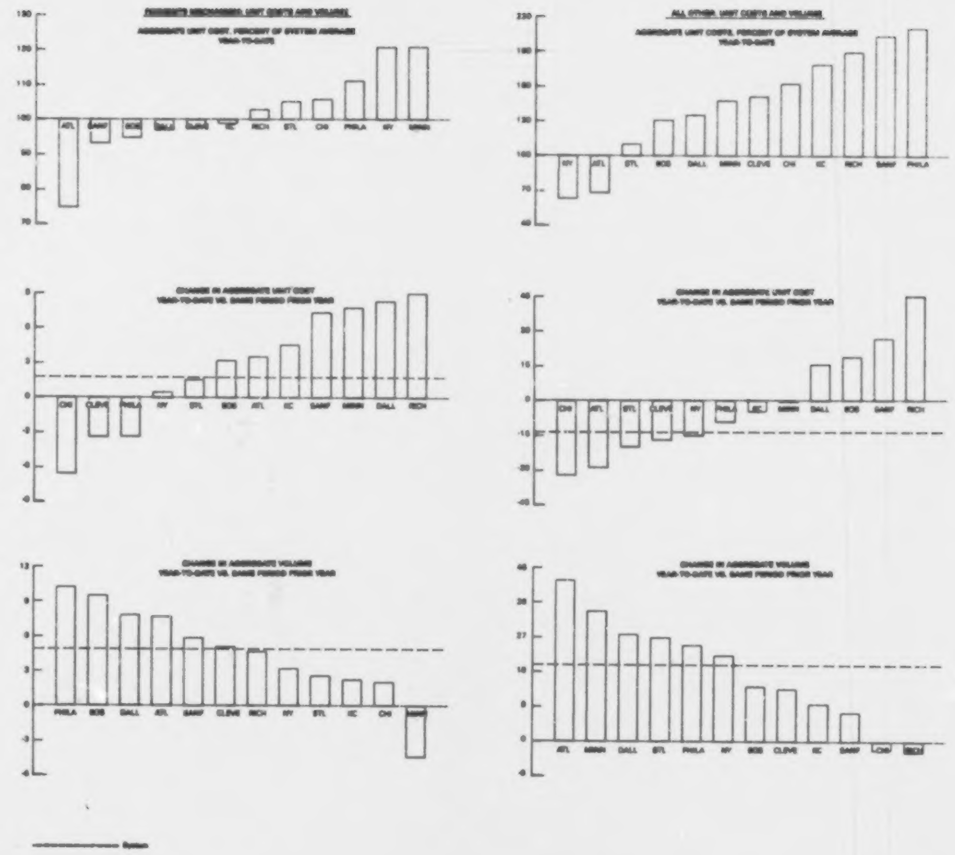

CHANGE IN AGGREGATE VOLUME
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
2
0
-2
-4
-6
-8
-10
MINN
SANF
STL
RICH
DALL
KC
ATL
PHILA
NY
CHI
CLEVE
BOS


CASH UNIT COSTS AND VOLUME
AGGREGATE UNIT COST, PERCENT OF SYSTEM AVERAGE
YEAR-TO-DATE
180
160
140
120
100
80
60
ATL
CHI
DALL
SANF
RICH
CLEVE
NY
PHILA
KC
STL
BOS
MINN


CHANGE IN AGGREGATE UNIT COST
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
21
14
7
0
-7
-14
-21
NY
MINN
KC
ATL
RICH
CHI
SANF
STL
CLEVE
DALL
PHILA
BOS


CHANGE IN AGGREGATE VOLUME
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
20
15
10
5
0
-5
-10
NY
RICH
ATL
SANF
MINN
CHI
KC
CLEVE
DALL
STL
BOS
PHILA

– – – – – – – System


PRODUCTS MECHANIZED: UNIT COSTS AND VOLUMES
AGGREGATE UNIT COST, PERCENT OF SYSTEM AVERAGE
YEAR-TO-DATE
130
120
110
100
90
80
70
ATL
SANF
BOS
DALL
CLEVE
KC
RICH
STL
CHI
PHILA
NY
MINN
CHANGE IN AGGREGATE UNIT COST
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
9
6
3
0
-3
-6
-9
CHI
CLEVE
PHILA
NY
STL
BOS
ATL
KC
SANF
MINN
DALL
RICH
CHANGE IN AGGREGATE VOLUME
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
12
9
6
3
0
-3
-6
PHILA
BOS
DALL
ATL
SANF
CLEVE
RICH
NY
STL
KC
CHI
MINN
ALL OTHER: UNIT COSTS AND VOLUMES
AGGREGATE UNIT COSTS, PERCENT OF SYSTEM AVERAGE
YEAR-TO-DATE
220
190
160
130
100
70
40
NY
ATL
STL
BOS
DALL
MINN
CLEVE
CHI
KC
RICH
SANF
PHILA
CHANGE IN AGGREGATE UNIT COST
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
40
30
15
0
-15
-30
-40
CHI
ATL
STL
CLEVE
NY
PHILA
KC
MINN
DALL
BOS
SANF
RICH
CHANGE IN AGGREGATE VOLUME
YEAR-TO-DATE VS. SAME PERIOD PRIOR YEAR
45
36
27
18
9
0
-9
ATL
MINN
DALL
STL
PHILA
NY
BOS
CLEVE
KC
SANF
CHI
RICH
System

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

NATIONWIDE AGGREGATE INDICES

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	97.29	102.74	100.99	102.33	97.34	104.51	7	97.34	96.01	107.23	100.11	104.51
NEW YORK	101.45	101.18	116.79	115.58	113.07	107.09	9	113.07	114.70	116.29	117.96	107.09
PHILADELPHIA	118.04	124.90	118.53	110.11	113.01	114.57	11	113.01	109.20	106.78	111.57	114.57
CLEVELAND	106.37	100.57	98.26	96.06	101.59	99.76	4	101.59	98.01	98.51	89.55	99.76
RICHMOND	95.04	97.52	96.43	96.96	96.93	103.51	6	96.93	95.63	95.65	99.37	103.51
ATLANTA	85.28	79.91	77.59	75.48	73.97	74.46	1	73.97	73.33	76.63	77.78	74.46
CHICAGO	107.51	104.68	106.38	104.99	111.19	102.58	5	111.19	109.10	101.97	98.33	102.58
ST. LOUIS	111.86	113.43	112.43	105.55	107.35	109.32	10	107.35	107.42	105.07	102.45	109.32
MINNEAPOLIS	110.63	111.67	116.05	121.72	121.53	124.74	12	121.53	121.18	120.83	123.18	124.74
KANSAS CITY	94.06	100.39	108.57	103.41	102.40	105.17	8	102.40	103.77	103.86	103.63	105.17
DALLAS	100.42	106.07	95.91	90.16	88.09	93.75	2	88.09	93.66	92.00	87.30	93.75
SAN FRANCISCO	87.79	92.44	98.22	94.07	92.43	95.79	3	92.43	93.75	92.76	97.03	95.79
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	79.50	99.24	100.00	99.53	97.39	105.40		97.39	88.99	104.17	107.36	105.40
NEW YORK	79.32	91.27	100.00	100.60	101.05	95.78		101.05	94.89	100.77	105.76	95.78
PHILADELPHIA	79.60	101.70	100.00	98.45	95.79	96.09		95.79	85.55	86.03	94.07	96.09
CLEVELAND	89.91	101.36	100.00	95.42	103.06	101.11		103.06	92.79	97.44	89.38	101.11
RICHMOND	81.77	98.30	100.00	98.49	100.90	108.24		100.90	93.08	97.42	102.67	108.24
ATLANTA	91.75	101.44	100.00	95.20	95.67	95.71		95.67	88.99	96.05	99.33	95.71
CHICAGO	82.61	95.78	100.00	97.99	104.68	97.55		104.68	98.14	95.22	94.23	97.55
ST. LOUIS	79.10	97.83	100.00	94.49	98.88	101.31		98.88	92.72	93.03	93.60	101.31
MINNEAPOLIS	79.51	94.57	100.00	101.72	104.25	106.17		104.25	98.21	100.61	103.09	106.17
KANSAS CITY	78.64	98.42	100.00	100.59	101.90	104.63		101.90	97.26	100.83	102.43	104.63
DALLAS	94.79	108.08	100.00	93.15	92.37	99.00		92.37	93.46	94.92	91.90	99.00
SAN FRANCISCO	75.85	96.52	100.00	98.11	98.89	103.06		98.89	92.85	96.43	104.23	103.06
SYSTEM	83.03	97.94	100.00	97.97	100.29	100.34		100.29	93.83	97.82	100.07	100.34
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	110.34	98.17	100.00	107.38	99.71	103.60		99.71	110.34	106.85	112.64	103.60
NEW YORK	103.72	99.64	100.00	104.70	98.82	104.71		98.82	107.79	105.69	107.30	104.71
PHILADELPHIA	108.53	95.56	100.00	111.06	103.24	107.09		103.24	113.69	112.84	114.98	107.09
CLEVELAND	104.85	95.95	100.00	106.50	100.23	103.55		100.23	108.73	103.37	113.67	103.55
RICHMOND	103.36	94.59	100.00	107.77	101.23	106.51		101.23	110.38	107.10	112.38	106.51
ATLANTA	98.96	93.35	100.00	139.48	104.85	112.98		104.85	111.91	107.81	113.76	112.98
CHICAGO	106.60	99.20	100.00	103.59	99.75	100.76		99.75	106.86	101.71	106.84	100.76
ST. LOUIS	112.72	96.42	100.00	112.55	107.25	109.00		107.25	114.68	112.98	115.29	109.00
MINNEAPOLIS	99.76	93.11	100.00	108.78	101.82	101.18		101.82	106.64	103.57	107.09	101.18
KANSAS CITY	109.52	98.91	100.00	102.59	99.73	101.85		99.73	104.16	101.68	104.81	101.85
DALLAS	96.67	92.35	100.00	109.65	105.92	112.15		105.92	108.58	108.71	115.39	112.15
SAN FRANCISCO	108.83	94.03	100.00	109.90	103.89	109.57		103.89	113.12	109.02	113.55	109.57
SYSTEM	102.82	96.11	100.00	106.60	101.16	105.90		101.16	108.94	105.84	110.47	105.90

The following changes became effective with First Quarter 1985 PACS reports:

(1) In the Aggregate Unit Cost and Aggregate Volume Time Series Indices, 1983 = 100 is used as the reference point year in lieu of 1979, as previously used.

(2) The former Electronic Funds Transfer Index is now shown as two sectors—a Transfer of Reserve Account Balances Index, and an Automated Clearing House Index.

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

FISCAL AGENCY

AGGREGATE UNIT COST INDEX (SYSTEM = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	99.36	103.05	92.22	92.34	88.07	103.50	5	88.07	86.70	52.63	101.63	103.50
NEW YORK	105.11	95.86	104.07	111.92	113.00	104.65	7	113.00	107.92	115.13	110.93	104.65
PHILADELPHIA	112.12	102.72	107.53	100.72	107.46	103.06	6	107.46	98.13	95.67	102.73	103.06
CLEVELAND	93.32	89.32	90.04	87.18	89.38	92.59	3	89.38	86.16	91.28	83.07	92.59
RICHMOND	101.61	99.06	96.96	102.37	104.78	111.37	11	104.78	100.79	102.62	100.16	111.37
ATLANTA	83.04	75.53	76.50	83.16	77.95	81.55	2	77.95	79.74	86.71	87.66	81.55
CHICAGO	105.00	107.87	98.37	101.26	100.41	97.74	4	100.41	113.35	93.87	97.15	97.74
ST. LOUIS	91.16	96.82	100.11	101.18	99.96	115.73	12	99.96	105.65	98.25	100.75	115.73
MINNEAPOLIS	101.22	127.16	128.01	122.10	126.76	107.25	9	126.76	114.74	115.84	128.94	107.25
KANSAS CITY	100.19	104.17	103.50	108.83	99.07	106.11	8	99.07	109.93	113.84	112.75	106.11
DALLAS	99.92	114.82	98.55	81.99	77.31	76.96	1	77.31	86.18	88.16	78.19	76.96
SAN FRANCISCO	103.35	107.86	115.32	107.03	113.77	107.99	10	113.77	102.18	105.84	106.52	107.99

AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	78.78	95.94	100.00	90.63	88.29	103.02		88.29	81.02	86.40	106.57	103.02
NEW YORK	71.60	84.94	100.00	99.55	101.05	103.65		101.05	90.60	97.77	108.96	103.65
PHILADELPHIA	75.86	89.68	100.00	89.94	97.64	94.66		97.64	88.70	79.68	99.07	94.66
CLEVELAND	76.01	95.69	100.00	94.56	96.08	100.87		96.08	90.19	94.80	97.42	100.87
RICHMOND	73.43	95.73	100.00	103.91	106.27	113.11		106.27	99.06	99.97	109.98	113.11
ATLANTA	76.40	91.32	100.00	104.64	98.08	103.75		98.08	98.02	105.56	118.01	103.75
CHICAGO	75.68	102.37	100.00	101.62	100.55	100.04		100.55	110.19	90.75	105.18	100.04
ST. LOUIS	62.19	88.29	100.00	101.48	102.07	117.03		102.07	103.62	93.38	107.88	117.03
MINNEAPOLIS	55.86	93.60	100.00	92.56	96.22	80.91		96.22	84.56	84.01	105.78	80.91
KANSAS CITY	66.74	93.01	100.00	102.64	94.72	101.32		94.72	99.71	103.39	114.32	101.32
DALLAS	85.42	117.84	100.00	90.92	84.10	86.08		84.10	93.69	95.06	91.57	86.08
SAN FRANCISCO	64.05	89.31	100.00	89.70	96.35	91.59		96.35	82.13	85.47	96.06	91.59
SYSTEM	70.43	93.29	100.00	97.76	97.76	100.48		97.76	94.09	93.07	106.08	100.48

AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	110.28	99.22	100.00	109.95	106.15	96.94		106.15	117.93	115.40	100.25	96.94
NEW YORK	111.62	108.87	100.00	106.06	96.06	90.72		96.06	112.80	112.03	102.76	90.72
PHILADELPHIA	98.87	102.18	100.00	108.35	103.62	97.93		103.62	112.07	117.52	100.18	97.93
CLEVELAND	113.53	103.37	100.00	105.63	107.77	98.81		107.77	109.38	104.49	100.91	98.81
RICHMOND	110.42	102.67	100.00	103.25	103.01	99.28		103.01	106.85	103.73	99.40	99.28
ATLANTA	106.99	102.89	100.00	98.86	100.97	95.47		100.97	101.31	100.26	92.98	95.47
CHICAGO	104.92	102.98	100.00	106.67	105.82	99.04		105.82	112.35	110.19	99.13	99.04
ST. LOUIS	113.12	99.98	100.00	109.11	103.34	100.61		103.34	112.32	118.06	102.72	100.61
MINNEAPOLIS	107.05	99.63	100.00	108.02	103.62	105.55		103.62	112.29	111.43	106.72	105.55
KANSAS CITY	105.68	103.44	100.00	104.99	111.57	106.88		111.57	106.58	106.36	95.65	106.88
DALLAS	88.40	89.82	100.00	106.75	115.53	110.92		115.53	106.80	103.78	102.09	110.92
SAN FRANCISCO	120.67	106.67	100.00	107.98	105.00	104.02		105.00	115.38	110.58	100.97	104.02
SYSTEM	110.17	103.31	100.00	105.60	103.86	98.45		103.86	110.14	108.99	99.42	98.45

SAVINGS BONDS

AGGREGATE UNIT COST INDEX (SYSTEM = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	113.37	104.43	103.57	98.22	98.71	106.66	7	98.71	93.39	98.17	101.60	106.66
NEW YORK	97.23	89.22	91.23	92.52	91.92	92.98	3	91.92	87.35	96.24	95.09	92.98
PHILADELPHIA	102.92	100.85	94.09	92.13	95.71	93.94	4	95.71	88.16	89.89	94.31	93.94
CLEVELAND	83.45	72.53	78.44	78.31	79.32	83.51	2	79.32	78.07	82.04	75.56	83.51
RICHMOND	101.47	102.34	98.70	101.24	108.08	108.00	8	108.08	102.78	97.68	94.02	108.00
ATLANTA	86.63	81.20	82.53	90.98	90.59	94.13	5	90.59	91.17	100.10	97.17	94.13
CHICAGO	102.15	111.27	108.16	115.48	116.03	112.49	10	116.03	128.42	106.76	100.86	112.49
ST. LOUIS	94.87	105.71	102.23	105.39	104.10	118.19	11	104.10	112.78	88.34	116.31	118.19
MINNEAPOLIS	108.42	140.11	135.94	129.12	139.88	102.55	6	139.88	119.25	122.79	131.86	102.55
KANSAS CITY	97.87	95.65	104.65	110.76	93.84	118.43	12	93.84	108.67	117.71	127.09	118.43
DALLAS	142.77	112.09	106.60	91.38	75.18	71.22	1	75.18	107.56	105.52	90.96	71.22
SAN FRANCISCO	108.03	122.53	123.62	108.85	122.75	110.93	9	122.75	101.07	108.37	102.70	110.93

AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	84.79	99.03	100.00	98.67	86.96	89.93		86.96	88.25	91.41	97.13	89.93
NEW YORK	84.36	100.48	100.00	99.19	94.11	90.78		94.11	94.15	103.26	105.91	90.78
PHILADELPHIA	88.89	110.57	100.00	93.67	92.66	87.18		92.66	90.44	91.20	99.74	87.18
CLEVELAND	84.92	95.73	100.00	98.09	93.04	95.35		93.04	98.48	102.59	99.38	95.35
RICHMOND	77.24	99.22	100.00	101.68	104.67	99.26		104.67	103.25	98.33	100.18	99.26
ATLANTA	82.34	98.73	100.00	112.36	103.50	102.52		103.50	108.63	118.79	110.08	102.52
CHICAGO	73.38	102.82	100.00	104.99	99.05	93.41		99.05	110.28	97.54	104.28	93.41
ST. LOUIS	70.21	108.16	100.00	100.13	95.19	103.46		95.19	108.52	84.65	113.39	103.46
MINNEAPOLIS	62.11	102.12	100.00	93.18	97.35	67.57		97.35	86.79	88.72	99.81	67.57
KANSAS CITY	73.38	92.25	100.00	102.27	85.68	100.45		85.68	100.17	108.00	110.64	100.45
DALLAS	107.17	102.69	100.00	83.71	68.99	64.21		68.99	94.40	92.85	83.52	64.21
SAN FRANCISCO	68.63	98.11	100.00	84.97	94.52	79.43		94.52	79.58	83.67	82.17	79.43
SYSTEM	77.56	99.43	100.00	98.00	93.61	89.56		93.61	98.74	98.16	101.92	89.56

AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	105.68	97.01	100.00	107.03	108.23	109.77		108.23	108.99	106.55	104.35	109.77
NEW YORK	97.94	91.27	100.00	103.26	108.17	105.07		108.17	105.25	98.60	101.01	105.07
PHILADELPHIA	95.65	89.27	100.00	101.22	104.10	106.24		104.10	103.75	98.21	98.81	106.24
CLEVELAND	115.77	101.96	100.00	96.70	110.53	98.39		110.53	95.06	89.74	91.23	98.39
RICHMOND	107.06	98.79	100.00	101.52	108.21	101.08		108.21	100.24	97.90	100.13	101.08
ATLANTA	95.72	92.51	100.00	93.83	96.69	96.35		96.69	92.83	91.69	94.12	96.35
CHICAGO	115.11	100.25	100.00	101.74	106.67	102.14		106.67	103.37	101.47	95.44	102.14
ST. LOUIS	117.08	101.10	100.00	106.51	106.75	107.52		106.75	102.50	111.60	105.19	107.52
MINNEAPOLIS	107.37	97.85	100.00	106.37	103.73	111.48		103.73	107.76	105.00	108.99	111.48
KANSAS CITY	101.81	99.01	100.00	107.18	121.45	121.00		121.45	104.11	102.57	100.41	121.00
DALLAS	66.17	92.58	100.00	102.09	125.04	122.14		125.04	94.35	94.11	94.05	122.14
SAN FRANCISCO	114.50	98.99	100.00	102.72	102.93	107.32		102.93	104.68	100.02	102.43	107.32
SYSTEM	105.94	97.45	100.00	101.26	107.99	105.52		107.99	101.15	97.93	97.98	105.52

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

OTHER TREASURY

AGGREGATE UNIT COST INDEX (SYSTEM = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	83.85	98.34	82.66	75.72	71.56	89.55	5	71.56	71.70	74.46	86.68	89.55
NEW YORK	106.10	89.09	109.03	133.39	150.32	122.72	11	150.32	129.03	137.31	117.99	122.72
PHILADELPHIA	136.62	119.64	116.07	99.24	107.60	116.97	9	107.60	102.27	89.42	101.70	116.97
CLEVELAND	106.22	105.04	97.81	84.84	91.04	87.52	4	91.04	81.24	89.27	79.54	87.52
RICHMOND	117.70	108.35	100.55	101.18	103.32	117.40	10	103.32	100.25	95.67	103.86	117.40
ATLANTA	79.34	77.39	78.21	81.14	68.75	71.63	1	68.75	70.70	87.53	88.54	71.63
CHICAGO	113.01	105.24	86.86	91.94	84.57	84.48	2	84.57	103.22	88.05	92.34	84.48
ST. LOUIS	92.92	94.33	87.20	77.58	77.89	103.97	7	77.89	77.09	83.21	72.25	103.97
MINNEAPOLIS	110.98	130.86	138.71	135.81	134.93	132.41	12	134.93	124.83	127.21	152.76	132.41
KANSAS CITY	92.98	99.61	88.38	106.87	96.17	93.84	6	96.17	112.10	111.84	107.29	93.84
DALLAS	73.52	190.02	105.74	84.27	74.94	86.36	3	74.94	96.61	93.50	78.28	86.36
SAN FRANCISCO	95.00	100.25	120.94	110.19	109.80	109.72	8	109.80	102.32	108.17	123.11	109.72

AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	63.25	97.75	100.00	81.10	87.70	121.68		87.70	67.26	69.95	110.09	121.68
NEW YORK	64.37	71.36	100.00	97.14	112.83	120.02		112.83	84.16	91.99	105.37	120.02
PHILADELPHIA	71.69	83.77	100.00	76.62	94.95	111.37		94.95	69.60	60.77	92.14	111.37
CLEVELAND	67.73	90.04	100.00	76.75	94.52	98.62		94.52	64.93	71.10	83.03	98.62
RICHMOND	72.89	88.52	100.00	89.37	104.35	120.80		104.35	77.60	74.00	110.02	120.80
ATLANTA	68.05	81.63	100.00	90.09	89.06	100.58		89.06	70.34	85.37	115.03	100.58
CHICAGO	82.80	99.59	100.00	95.45	101.17	110.49		101.17	94.93	80.59	109.60	110.49
ST. LOUIS	64.66	86.69	100.00	82.09	97.70	136.20		97.70	76.20	75.90	86.56	136.20
MINNEAPOLIS	49.72	70.45	100.00	87.13	97.04	107.76		97.04	70.52	72.09	117.08	107.76
KANSAS CITY	62.23	80.07	100.00	105.23	107.99	115.70		107.99	94.36	97.93	127.30	115.70
DALLAS	40.71	138.91	100.00	73.30	72.07	93.33		72.07	71.09	69.93	79.70	93.33
SAN FRANCISCO	49.31	70.38	100.00	77.29	86.09	97.38		86.09	62.01	67.01	102.54	97.38
SYSTEM	63.54	82.99	100.00	89.71	100.10	114.40		100.10	70.99	80.48	105.37	114.40

AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	127.65	103.64	100.00	120.09	104.66	83.01		104.66	106.64	104.25	102.20	83.01
NEW YORK	124.71	124.62	100.00	114.19	87.82	78.48		87.82	125.57	120.80	112.57	78.48
PHILADELPHIA	100.97	123.41	100.00	132.26	103.06	88.63		103.06	142.01	160.65	114.50	88.63
CLEVELAND	130.36	118.31	100.00	134.15	108.07	107.39		108.07	157.09	147.03	123.20	107.39
RICHMOND	123.92	114.41	100.00	120.77	106.60	89.68		106.60	132.26	141.05	102.76	89.68
ATLANTA	139.13	132.47	100.00	114.04	106.94	97.20		106.94	126.62	127.02	97.97	97.20
CHICAGO	101.37	116.73	100.00	123.55	103.03	97.88		103.03	143.32	138.42	108.43	97.88
ST. LOUIS	121.04	101.74	100.00	133.66	109.45	92.54		109.45	146.49	156.14	122.57	92.54
MINNEAPOLIS	121.07	111.82	100.00	128.46	110.65	92.17		110.65	145.42	146.03	110.96	92.17
KANSAS CITY	126.44	122.40	100.00	110.50	100.70	95.24		100.70	125.63	125.35	90.32	95.24
DALLAS	265.55	98.49	100.00	122.24	115.62	102.17		115.62	121.29	133.16	118.09	102.17
SAN FRANCISCO	171.27	141.92	100.00	126.24	111.99	97.11		111.99	153.16	136.83	100.97	97.11
SYSTEM	130.07	120.31	100.00	120.10	100.01	88.39		100.01	135.52	137.53	107.34	88.39

OTHER FISCAL AGENCY

AGGREGATE UNIT COST INDEX (SYSTEM = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	103.84	107.58	113.92	110.55	102.10	119.15	11	102.10	101.43	115.69	123.97	119.15
NEW YORK	116.80	118.92	117.02	118.15	100.64	104.08	5	100.64	115.09	118.94	129.58	104.08
PHILADELPHIA	105.95	86.79	119.11	116.76	124.67	105.38	8	124.67	109.73	114.92	118.26	105.38
CLEVELAND	108.33	112.64	107.44	104.58	107.00	113.09	10	107.00	104.68	108.30	97.01	113.09
RICHMOND	92.91	92.64	93.06	104.32	101.83	111.39	9	101.83	99.05	112.92	103.57	111.39
ATLANTA	82.23	70.05	75.32	75.31	73.31	77.46	1	73.31	71.87	76.65	79.83	77.46
CHICAGO	102.94	105.77	96.49	93.68	96.64	94.16	3	96.64	105.27	84.44	88.61	94.16
ST. LOUIS	87.20	92.07	107.91	120.70	117.95	123.59	12	117.95	127.87	119.31	117.98	123.59
MINNEAPOLIS	84.92	109.44	115.35	105.71	107.08	99.24	4	107.08	103.41	100.77	111.14	99.24
KANSAS CITY	108.59	115.28	113.57	100.52	107.65	104.22	6	107.65	109.56	112.07	105.04	104.22
DALLAS	93.19	100.65	77.27	75.88	79.40	78.46	2	79.40	74.06	78.33	71.95	78.46
SAN FRANCISCO	105.30	99.39	102.29	103.59	108.32	104.53	7	108.32	103.07	102.30	100.69	104.53

AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	62.48	89.37	100.00	103.21	90.50	110.54		90.50	95.92	106.86	122.00	110.54
NEW YORK	68.09	93.20	100.00	106.21	92.30	96.08		92.30	104.22	107.00	123.40	96.08
PHILADELPHIA	60.64	68.54	100.00	104.76	106.97	95.95		106.97	100.79	100.42	110.71	95.95
CLEVELAND	60.40	99.37	100.00	105.50	101.87	113.98		101.87	105.40	108.27	106.38	113.98
RICHMOND	69.00	96.09	100.00	117.88	109.67	124.09		109.67	113.76	127.44	121.51	124.09
ATLANTA	74.00	89.30	100.00	105.89	97.66	107.96		97.66	101.42	107.30	110.57	107.96
CHICAGO	72.32	103.91	100.00	102.07	101.03	102.52		101.03	115.90	92.33	102.39	102.52
ST. LOUIS	55.32	81.57	100.00	118.80	110.08	121.31		110.08	126.12	117.23	122.09	121.31
MINNEAPOLIS	49.66	91.62	100.00	96.21	93.74	86.59		93.74	94.51	90.45	106.44	86.59
KANSAS CITY	64.12	96.41	100.00	101.35	95.67	94.26		95.67	103.22	103.56	103.72	94.26
DALLAS	79.95	124.12	100.00	103.10	103.19	105.21		103.19	100.73	106.05	101.79	105.21
SAN FRANCISCO	69.58	92.66	100.00	105.70	106.15	104.32		106.15	105.27	104.06	107.30	104.32
SYSTEM	68.38	95.22	100.00	105.09	100.69	105.16		100.69	106.40	105.22	111.60	105.16

AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	98.22	95.95	100.00	97.62	105.25	91.83		105.25	98.37	93.53	93.33	91.83
NEW YORK	109.95	108.12	100.00	92.82	97.66	95.78		97.66	95.14	93.00	84.66	95.78
PHILADELPHIA	104.06	102.31	100.00	92.68	103.57	90.19		103.57	90.82	89.32	87.01	90.19
CLEVELAND	98.74	96.37	100.00	99.62	103.57	91.27		103.57	97.60	97.14	100.15	91.27
RICHMOND	106.73	100.74	100.00	94.52	94.85	99.68		94.85	99.08	87.62	96.54	99.68
ATLANTA	103.88	100.04	100.00	95.60	101.91	92.55		101.91	96.50	98.39	89.51	92.55
CHICAGO	96.09	96.49	100.00	100.96	106.84	94.67		106.84	99.04	100.22	94.94	94.67
ST. LOUIS	103.66	97.70	100.00	95.42	97.29	96.29		97.29	97.32	98.40	88.65	96.29
MINNEAPOLIS	98.45	95.72	100.00	97.20	99.01	104.26		99.01	97.43	97.73	94.94	104.26
KANSAS CITY	97.72	96.97	100.00	100.20	109.98	102.70		109.98	97.74	98.13	94.95	102.70
DALLAS	82.56	84.89	100.00	105.09	106.80	104.48		106.80	108.52	102.84	105.39	104.48
SAN FRANCISCO	101.91	97.22	100.00	101.19	102.45	102.41		102.45	101.10	101.85	99.37	102.41
SYSTEM	100.82	97.53	100.00	98.09	102.52	96.99		102.52	98.54	97.02	94.28	96.99

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	139.43	132.23	113.03	127.68	115.16	134.04	11	115.16	112.15	144.67	137.73	134.04
NEW YORK	115.85	105.44	118.39	126.92	129.97	112.19	7	129.97	129.79	122.77	125.11	112.19
PHILADELPHIA	102.26	105.62	99.14	102.70	99.28	120.08	8	99.28	103.46	102.28	105.24	120.08
CLEVELAND	118.72	101.89	97.36	95.15	97.39	102.75	6	97.39	99.87	94.83	89.56	102.75
RICHMOND	90.22	98.09	93.04	93.08	94.54	95.13	5	94.54	91.32	89.42	97.16	95.13
ATLANTA	95.15	91.40	85.78	75.65	72.97	70.83	1	72.97	72.98	76.33	79.92	70.83
CHICAGO	81.09	76.98	78.93	79.71	82.43	82.04	2	82.43	81.92	81.72	74.37	82.04
ST. LOUIS	119.37	114.26	117.66	115.06	117.24	123.94	10	117.24	115.96	115.80	111.92	123.94
MINNEAPOLIS	145.72	167.80	181.24	182.32	198.61	174.30	12	198.61	197.07	167.48	170.08	174.30
KANSAS CITY	101.90	109.57	124.28	123.32	127.73	122.82	9	127.73	126.77	116.33	122.90	122.82
DALLAS	87.59	105.61	90.29	84.20	82.94	88.50	3	82.94	87.21	87.21	79.95	88.50
SAN FRANCISCO	71.16	83.53	87.53	85.82	84.14	88.65	4	84.14	85.73	85.03	86.55	88.65
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	99.74	110.56	100.00	109.61	110.40	125.65		110.40	85.77	124.63	119.59	125.65
NEW YORK	80.67	84.71	100.00	103.32	117.91	97.20		117.91	95.11	99.78	102.66	97.20
PHILADELPHIA	85.12	100.98	100.00	100.03	108.17	125.60		108.17	90.15	99.54	103.89	125.60
CLEVELAND	99.32	98.79	100.00	95.03	108.64	112.39		108.64	88.59	94.81	90.68	112.39
RICHMOND	78.89	98.79	100.00	95.46	107.99	104.95		107.99	84.03	92.23	100.12	104.95
ATLANTA	92.17	101.81	100.00	84.19	90.24	84.82		90.24	73.74	84.70	89.04	84.82
CHICAGO	88.87	92.32	100.00	97.47	112.57	109.83		112.57	89.65	100.15	91.75	109.83
ST. LOUIS	82.84	91.48	100.00	95.07	109.48	111.91		109.48	85.25	95.01	93.72	111.91
MINNEAPOLIS	65.40	87.08	100.00	97.76	119.45	103.27		119.45	93.96	89.37	93.33	103.27
KANSAS CITY	66.58	82.89	100.00	96.30	111.43	104.22		111.43	88.21	91.01	97.13	104.22
DALLAS	79.27	110.48	100.00	90.13	99.13	103.14		99.13	83.25	93.54	86.62	103.14
SAN FRANCISCO	66.94	90.30	100.00	93.89	103.70	105.06		103.70	84.52	93.38	95.70	105.06
SYSTEM	82.05	94.61	100.00	96.46	107.67	104.00		107.67	86.83	96.57	97.28	104.00
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	91.68	89.09	100.00	100.83	91.68	88.97		91.68	119.11	104.30	120.23	88.97
NEW YORK	94.84	100.61	100.00	104.77	91.68	109.02		91.68	109.11	103.69	114.60	109.02
PHILADELPHIA	82.16	90.77	100.00	107.34	95.50	87.58		95.50	113.89	104.51	115.45	87.58
CLEVELAND	86.33	92.78	100.00	110.39	94.54	99.05		94.54	114.14	108.95	123.91	99.05
RICHMOND	91.80	91.32	100.00	112.80	92.04	103.78		92.04	118.84	113.96	123.17	103.78
ATLANTA	84.28	92.01	100.00	116.82	103.96	114.13		103.96	124.19	113.43	125.70	114.13
CHICAGO	87.24	92.05	100.00	111.75	91.21	98.11		91.21	118.72	108.04	129.05	98.11
ST. LOUIS	90.00	95.31	100.00	103.57	88.68	87.96		88.68	114.83	101.86	109.33	87.96
MINNEAPOLIS	87.13	92.88	100.00	111.54	90.66	98.52		90.66	114.02	116.81	124.67	98.52
KANSAS CITY	100.04	104.18	100.00	106.44	91.17	95.61		91.17	110.70	109.20	114.69	95.61
DALLAS	83.82	85.56	100.00	111.10	97.02	98.21		97.02	117.39	107.25	122.76	98.21
SAN FRANCISCO	88.36	92.25	100.00	117.30	100.00	108.80		100.00	123.53	115.44	130.21	108.80
SYSTEM	89.23	93.63	100.00	110.80	94.91	102.42		94.91	117.23	109.00	122.08	102.42

CURRENCY

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	110.86	118.07	104.90	116.61	105.79	123.26	11	105.79	102.31	129.98	126.81	123.26
NEW YORK	115.81	103.95	116.79	125.47	128.56	109.44	7	128.56	127.78	121.65	123.94	109.44
PHILADELPHIA	96.44	105.18	96.08	101.01	96.12	117.18	10	96.12	102.97	100.28	103.89	117.18
CLEVELAND	102.45	91.45	90.38	90.53	91.12	100.87	6	91.12	93.72	91.18	86.69	100.87
RICHMOND	97.51	102.80	98.91	98.31	97.52	98.79	5	97.52	96.65	96.65	102.14	98.79
ATLANTA	107.27	104.66	98.55	85.67	82.28	81.66	1	82.28	83.88	85.35	90.39	81.66
CHICAGO	84.76	79.77	78.83	79.44	82.43	82.72	2	82.43	81.74	81.52	73.96	82.72
ST. LOUIS	120.19	109.81	106.03	106.96	105.14	110.24	8	105.14	108.85	110.17	104.04	110.24
MINNEAPOLIS	148.88	166.53	167.05	164.90	182.44	165.14	12	182.44	176.85	159.33	153.50	165.14
KANSAS CITY	97.63	105.29	117.18	117.37	120.86	115.42	9	120.86	122.15	110.57	116.34	115.42
DALLAS	93.32	106.47	87.54	83.75	81.38	89.35	4	81.38	87.71	87.84	79.32	89.35
SAN FRANCISCO	74.05	83.66	89.45	84.81	86.48	89.23	3	86.48	83.76	83.63	85.67	89.23
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	88.32	107.86	100.00	106.72	107.75	118.06		107.75	84.77	118.45	116.72	118.06
NEW YORK	82.06	85.29	100.00	103.14	117.61	94.15		117.61	95.09	99.57	102.46	94.15
PHILADELPHIA	83.08	104.98	100.00	100.93	106.89	122.50		106.89	93.15	99.77	108.40	122.50
CLEVELAND	94.73	96.96	100.00	96.16	107.72	112.13		107.72	90.12	96.43	92.61	112.13
RICHMOND	82.38	99.59	100.00	95.42	105.33	100.35		105.33	84.92	93.41	99.70	100.35
ATLANTA	90.97	101.77	100.00	83.46	89.13	83.25		89.13	73.98	82.80	88.56	83.25
CHICAGO	89.85	96.96	100.00	96.78	111.72	105.43		111.72	90.11	98.85	90.58	105.43
ST. LOUIS	94.73	99.24	100.00	96.85	105.94	104.47		105.94	89.22	99.32	94.73	104.47
MINNEAPOLIS	74.28	95.53	100.00	95.92	116.68	99.32		116.68	91.80	91.17	88.72	99.32
KANSAS CITY	69.63	86.10	100.00	96.15	110.20	98.97		110.20	90.60	98.21	95.86	98.97
DALLAS	89.08	116.54	100.00	91.85	99.32	102.55		99.32	87.07	95.47	87.48	102.55
SAN FRANCISCO	69.18	89.62	100.00	91.82	103.29	100.23		103.29	81.38	89.37	92.47	100.23
SYSTEM	83.57	95.03	100.00	96.00	106.84	100.47		106.84	86.91	95.59	96.55	100.47
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	88.04	89.48	100.00	111.64	94.31	96.05		94.31	119.14	108.36	124.75	96.05
NEW YORK	93.13	100.25	100.00	106.15	92.68	113.64		92.68	110.25	104.75	116.91	113.64
PHILADELPHIA	80.87	88.04	100.00	108.79	99.07	92.28		99.07	112.83	104.99	118.26	92.28
CLEVELAND	86.14	93.32	100.00	114.14	97.97	105.06		97.97	114.97	111.82	131.80	105.06
RICHMOND	91.96	90.86	100.00	113.49	94.16	108.21		94.16	118.82	114.82	126.98	108.21
ATLANTA	82.47	91.14	100.00	118.16	105.64	116.75		105.64	123.57	115.26	128.16	116.75
CHICAGO	85.74	91.32	100.00	112.25	91.39	101.04		91.39	117.75	107.47	132.39	101.04
ST. LOUIS	85.21	91.90	100.00	106.37	95.21	96.83		95.21	114.76	101.47	114.04	96.83
MINNEAPOLIS	83.33	89.93	100.00	115.07	95.82	107.90		95.82	115.47	113.45	135.55	107.90
KANSAS CITY	92.79	99.68	100.00	109.93	94.63	102.76		94.63	111.24	113.24	120.60	102.76
DALLAS	79.88	82.13	100.00	112.03	97.01	102.93		97.01	115.79	[illegible]	120.13	102.93
SAN FRANCISCO	87.99	93.06	100.00	119.95	98.90	113.93		98.90	125.99	[illegible]	135.69	113.93
SYSTEM	87.61	92.87	100.00	112.54	96.33	107.30		96.33	112.35	[illegible]	126.05	107.30

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

COIN

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	264.24	197.58	148.69	180.40	159.63	188.10	10	159.63	156.66	216.65	191.46	188.10
NEW YORK	112.40	118.59	132.04	140.45	142.62	141.30	8	142.62	149.20	132.61	136.64	141.30
PHILADELPHIA	133.41	107.75	115.84	112.40	119.94	138.60	7	119.94	106.05	112.90	113.35	138.60
CLEVELAND	169.47	134.66	117.21	109.63	116.63	108.10	6	116.63	118.30	105.52	99.22	108.10
RICHMOND	61.59	81.01	76.14	73.92	83.15	81.63	2	83.15	72.22	65.48	77.23	81.63
ATLANTA	57.53	47.88	43.40	39.75	38.92	34.79	1	38.92	37.16	43.53	40.10	34.79
CHICAGO	68.84	65.94	79.29	80.75	82.45	83.24	3	82.45	82.65	82.45	76.12	83.24
ST. LOUIS	116.38	131.37	166.73	151.91	182.77	196.02	11	182.77	147.20	138.00	149.47	196.02
MINNEAPOLIS	138.93	171.26	218.36	225.62	247.00	200.55	12	247.00	254.81	186.01	228.12	200.55
KANSAS CITY	115.63	124.25	151.61	148.90	157.39	154.99	9	157.39	145.43	140.77	152.92	154.99
DALLAS	69.87	103.09	99.37	85.68	87.89	86.00	5	87.89	85.62	86.50	82.34	86.00
SAN FRANCISCO	57.99	82.92	79.27	88.39	75.09	85.95	4	75.09	95.55	91.99	91.26	85.95
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	134.60	118.89	100.00	119.56	119.66	155.57		119.66	88.89	147.19	130.00	155.57
NEW YORK	64.52	80.36	100.00	104.83	120.39	131.62		120.39	95.33	101.46	104.47	131.62
PHILADELPHIA	87.23	83.22	100.00	95.62	115.40	147.16		115.40	77.23	98.45	98.79	147.16
CLEVELAND	109.51	102.80	100.00	92.17	110.91	113.42		110.91	85.15	90.94	85.46	113.42
RICHMOND	61.26	95.19	100.00	95.67	121.71	131.85		121.71	80.02	86.87	102.40	131.85
ATLANTA	100.40	98.73	100.00	90.26	99.95	98.58		99.95	72.20	101.32	93.30	98.58
CHICAGO	65.76	74.40	100.00	100.36	115.89	129.11		115.89	87.93	105.04	96.91	129.11
ST. LOUIS	52.87	70.50	100.00	89.79	122.17	145.10		122.17	74.48	83.61	90.50	145.10
MINNEAPOLIS	48.19	70.17	100.00	101.82	126.07	112.95		126.07	98.45	86.05	105.47	112.95
KANSAS CITY	57.76	73.33	100.00	96.78	115.70	125.72		115.70	80.93	93.79	101.83	125.72
DALLAS	53.25	92.81	100.00	84.97	98.58	106.44		98.58	72.69	87.92	83.65	106.44
SAN FRANCISCO	55.41	93.60	100.00	109.89	105.58	133.35		105.58	101.70	117.23	116.23	133.35
SYSTEM	75.74	89.47	100.00	98.55	111.45	122.99		111.45	84.36	101.01	100.95	122.99
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	90.37	91.03	100.00	100.12	83.52	68.65		83.52	119.00	91.74	106.23	68.65
NEW YORK	106.55	103.47	100.00	96.41	84.20	74.61		84.20	108.47	95.76	97.19	74.61
PHILADELPHIA	91.10	106.34	100.00	100.76	79.31	65.61		79.31	118.70	102.33	102.69	65.61
CLEVELAND	86.61	91.66	100.00	102.16	87.04	85.61		87.04	112.32	102.67	106.63	85.61
RICHMOND	90.15	93.50	100.00	105.25	82.47	83.71		82.47	118.97	113.68	105.88	83.71
ATLANTA	97.81	98.76	100.00	106.72	91.25	95.16		91.25	128.83	99.65	107.16	95.16
CHICAGO	95.01	95.71	100.00	109.84	90.48	87.15		90.48	122.46	110.24	116.14	87.15
ST. LOUIS	109.75	108.20	100.00	96.05	71.15	62.77		71.15	113.55	102.89	96.62	62.77
MINNEAPOLIS	97.85	100.77	100.00	104.47	80.33	80.47		80.33	111.11	123.55	102.90	80.47
KANSAS CITY	125.63	119.89	100.00	96.05	80.87	74.38		80.87	109.07	97.18	97.09	74.38
DALLAS	94.26	98.11	100.00	108.42	97.06	83.54		97.06	122.05	107.44	107.10	83.54
SAN FRANCISCO	91.70	88.47	100.00	104.42	105.30	86.11		105.30	111.61	97.11	103.64	86.11
SYSTEM	96.70	97.33	100.00	103.46	88.91	82.20		88.91	116.73	102.90	105.31	82.20

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

PAYMENTS MECHANISM

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	85.72	95.20	98.22	96.06	93.56	94.82	3	93.56	92.66	98.75	98.78	94.82
NEW YORK	116.82	119.90	125.54	127.20	122.10	120.78	11	122.10	125.04	129.87	131.47	120.78
PHILADELPHIA	120.29	133.11	126.07	113.05	117.82	111.07	10	117.82	117.87	108.21	114.59	111.07
CLEVELAND	104.33	99.77	97.76	98.19	103.64	97.81	5	103.64	100.71	98.21	90.92	97.81
RICHMOND	95.32	96.10	97.09	96.35	95.86	102.87	7	95.86	95.11	95.90	98.37	102.87
ATLANTA	82.41	76.97	75.18	74.32	73.54	74.85	1	73.54	72.36	75.00	76.20	74.85
CHICAGO	110.20	107.54	111.38	108.84	115.65	105.80	9	115.65	111.90	105.64	102.75	105.80
ST. LOUIS	110.53	114.03	113.49	104.14	106.65	105.16	8	106.65	104.91	104.68	100.37	105.16
MINNEAPOLIS	107.75	101.77	106.85	114.96	113.20	120.84	12	113.20	114.59	116.42	115.80	120.84
KANSAS CITY	87.30	91.55	92.96	96.09	95.82	98.83	6	95.82	96.29	96.69	95.62	98.83
DALLAS	109.66	103.08	97.22	92.51	91.27	96.77	4	91.27	95.64	93.43	89..2	96.77
SAN FRANCISCO	86.02	89.07	83.82	92.58	89.15	93.25	2	89.15	92.89	90.98	96.96	93.25
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	72.22	95.20	100.00	97.68	94.90	97.95		94.90	92.38	101.10	101.95	97.95
NEW YORK	78.95	95.21	100.00	101.25	96.46	96.93		96.46	97.25	103.47	107.68	96.93
PHILADELPHIA	78.92	102.81	100.00	89.77	92.96	89.84		92.96	86.87	86.60	92.73	89.84
CLEVELAND	91.36	102.08	100.00	98.74	104.17	100.65		104.17	99.07	99.47	92.75	100.65
RICHMOND	82.67	97.44	100.00	98.15	97.65	107.01		97.65	94.88	98.50	101.46	107.01
ATLANTA	94.27	102.32	100.00	97.78	96.65	100.08		96.65	93.09	99.54	101.53	100.08
CHICAGO	83.86	95.42	100.00	97.72	103.46	96.66		103.46	98.47	95.37	93.77	96.66
ST. LOUIS	79.27	98.91	100.00	93.84	96.83	98.38		96.83	92.56	94.01	92.11	98.38
MINNEAPOLIS	85.93	94.68	100.00	105.79	104.58	112.71		104.58	103.53	108.03	107.11	112.71
KANSAS CITY	81.09	98.77	100.00	101.95	101.82	106.51		101.82	100.29	103.10	102.58	106.51
DALLAS	96.12	105.19	100.00	95.18	93.53	101.32		93.53	96.58	96.60	94.08	101.32
SAN FRANCISCO	80.53	100.58	100.00	102.73	98.68	105.93		98.68	100.22	101.68	109.99	105.93
SYSTEM	84.51	98.95	100.00	99.52	99.39	101.17		99.39	97.42	100.12	101.11	101.17
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	121.04	102.15	100.00	105.58	100.90	110.48		100.90	104.53	104.92	111.97	110.48
NEW YORK	105.33	96.25	100.00	103.31	100.46	103.69		100.46	104.82	103.85	104.49	103.69
PHILADELPHIA	115.78	95.64	100.00	112.42	105.90	116.74		105.90	112.78	113.60	117.44	116.74
CLEVELAND	106.77	95.39	100.00	101.95	98.61	103.62		98.61	101.62	100.51	107.06	103.62
RICHMOND	106.78	94.20	100.00	107.89	104.29	109.17		104.29	108.38	105.71	11 .59	109.17
ATLANTA	96.32	93.27	100.00	108.03	104.75	112.77		104.75	108.64	106.65	112.09	112.77
CHICAGO	107.39	99.80	100.00	102.11	99.72	101.76		99.72	103.00	100.36	105.36	101.76
ST. LOUIS	117.05	96.43	100.00	113.59	111.22	114.13		111.22	113.92	111.75	117.49	114.13
MINNEAPOLIS	95.00	91.01	100.00	101.33	102.36	97.88		102.36	102.51	97.72	102.71	97.88
KANSAS CITY	109.74	97.18	100.00	101.36	99.72	101.99		99.72	101.90	99.39	104.33	101.99
DALLAS	101.25	94.19	100.00	108.68	105.29	113.56		105.29	106.56	108.09	114.77	113.56
SAN FRANCISCO	99.12	90.98	100.00	107.23	104.32	110.42		104.32	108.12	105.48	111.00	110.42
SYSTEM	104.56	95.10	100.00	104.73	101.85	106.84		101.85	105.16	103.40	108.51	106.84

TRANSFER OF RESERVE ACCOUNT BALANCES

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	60.88	64.00	63.71	75.64	68.58	83.27	1	68.58	70.89	83.52	79.30	83.27
NEW YORK	109.77	109.00	118.22	100.25	105.55	85.77	2	105.55	98.69	106.87	91.31	85.77
PHILADELPHIA	123.10	132.46	147.20	108.60	109.93	106.65	8	109.93	107.07	106.52	110.85	106.65
CLEVELAND	110.61	77.42	86.64	97.85	118.18	89.15	3	118.18	118.77	85.42	73.90	89.15
RICHMOND	99.12	78.98	78.29	114.18	112.86	131.96	11	112.86	109.20	100.13	132.36	131.96
ATLANTA	62.09	73.11	72.82	84.89	81.72	97.80	7	81.72	84.38	93.28	80.88	97.80
CHICAGO	135.17	131.62	143.26	119.58	138.06	108.24	9	138.06	127.18	111.90	103.12	108.24
ST. LOUIS	72.72	83.26	68.44	119.01	121.88	95.22	5	121.88	125.12	125.99	105.24	95.22
MINNEAPOLIS	170.18	177.26	144.58	167.04	165.76	182.41	12	165.76	173.97	144.40	162.45	182.41
KANSAS CITY	94.88	86.82	66.07	72.68	71.19	94.38	4	71.19	73.81	75.75	70.32	94.38
DALLAS	105.59	115.86	98.70	94.24	88.09	97.27	6	88.09	98.38	96.91	93.63	97.27
SAN FRANCISCO	69.00	81.72	79.50	92.85	64.21	108.64	10	64.21	77.42	81.80	139.35	108.64
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	92.09	108.17	100.00	110.25	99.78	117.39		99.78	99.80	116.64	124.35	117.39
NEW YORK	89.47	58.85	100.00	78.74	82.75	65.16		82.75	74.87	80.42	77.15	65.16
PHILADELPHIA	80.50	95.70	100.00	68.55	69.22	65.06		69.22	65.24	64.38	75.23	65.06
CLEVELAND	123.01	95.03	100.00	104.86	126.42	92.41		126.42	122.95	87.71	85.21	92.41
RICHMOND	121.99	107.28	100.00	135.41	133.59	151.37		133.59	125.10	113.78	168.88	151.37
ATLANTA	82.11	106.77	100.00	108.24	104.01	120.62		104.01	103.87	113.96	110.95	120.62
CHICAGO	90.91	97.71	100.00	77.50	89.31	67.85		89.31	79.62	69.49	71.90	67.85
ST. LOUIS	102.39	129.38	100.00	161.47	165.06	124.96		165.06	163.97	163.78	153.61	124.96
MINNEAPOLIS	113.36	130.39	100.00	107.27	106.26	113.31		106.26	107.92	102.39	112.38	113.31
KANSAS CITY	141.28	139.74	100.00	102.13	99.86	128.24		99.86	100.19	102.00	106.32	128.24
DALLAS	103.08	124.83	100.00	88.55	82.71	88.51		82.71	89.36	87.35	94.76	88.51
SAN FRANCISCO	83.63	109.31	100.00	108.43	74.86	122.72		74.86	87.33	91.53	175.06	122.72
SYSTEM	96.36	106.35	100.00	92.05	92.68	89.81		92.68	89.69	88.96	99.99	89.81
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	76.15	94.59	100.00	105.05	102.58	107.78		102.58	105.58	105.40	106.63	107.78
NEW YORK	78.38	91.48	100.00	107.83	102.31	111.68		102.31	107.58	109.28	112.16	111.68
PHILADELPHIA	76.10	92.81	100.00	111.37	109.25	117.52		109.25	109.87	112.28	118.07	117.52
CLEVELAND	88.17	99.04	100.00	109.82	104.61	111.63		104.61	107.11	110.89	116.65	111.63
RICHMOND	79.58	94.01	100.00	106.84	102.77	108.59		102.77	107.51	108.36	104.73	108.59
ATLANTA	82.90	93.70	100.00	106.38	103.22	105.60		103.22	107.14	106.51	108.63	105.60
CHICAGO	86.71	95.87	100.00	105.01	102.49	105.20		102.49	106.74	106.24	104.56	105.20
ST. LOUIS	90.70	98.87	100.00	106.31	102.97	113.64		102.97	106.65	104.10	111.51	113.64
MINNEAPOLIS	84.25	92.12	100.00	111.72	106.05	112.12		106.05	112.41	113.30	115.12	112.12
KANSAS CITY	79.99	93.53	100.00	106.29	103.30	109.17		103.30	106.19	106.89	108.77	109.17
DALLAS	80.25	93.96	100.00	112.91	107.70	118.67		107.70	111.72	115.94	116.27	118.67
SAN FRANCISCO	77.07	88.13	100.00	116.21	109.01	121.24		109.01	115.66	118.60	121.58	121.24
SYSTEM	80.94	93.30	100.00	108.57	104.16	111.59		104.16	108.55	109.78	111.79	111.59

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

COMMERCIAL CHECKS

AGGREGATE UNIT COST INDEX (SYSTEM = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	86.92	102.41	100.94	102.63	101.07	99.96	6	101.07	99.21	104.34	105.35	99.96
NEW YORK	117.08	123.76	127.54	134.11	125.24	129.69	12	125.24	131.26	135.11	144.53	129.69
PHILADELPHIA	122.63	140.26	127.21	116.99	120.96	115.14	10	120.96	115.39	112.27	119.47	115.14
CLEVELAND	103.38	95.74	97.22	97.50	101.50	97.80	4	101.50	97.53	99.02	92.34	97.80
RICHMOND	96.63	101.19	102.88	97.91	98.26	103.68	7	98.26	96.42	98.35	98.61	103.68
ATLANTA	82.95	74.52	72.30	70.49	69.50	71.07	1	69.50	67.90	70.96	73.42	71.07
CHICAGO	105.01	103.19	108.49	107.28	112.96	105.94	9	112.96	110.40	104.42	101.75	105.94
ST. LOUIS	114.56	116.37	112.35	100.66	104.60	105.52	8	104.60	104.62	100.19	95.44	105.52
MINNEAPOLIS	104.26	95.11	102.30	110.61	108.40	115.23	11	108.40	111.16	112.39	110.74	115.23
KANSAS CITY	85.58	90.87	93.40	96.43	95.87	98.55	5	95.87	96.03	97.04	96.81	98.55
DALLAS	109.70	101.00	97.06	91.88	92.02	94.58	3	92.02	96.09	92.45	87.37	94.58
SAN FRANCISCO	90.38	91.07	83.57	93.39	93.85	91.22	2	93.85	95.49	92.69	91.61	91.22

AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	67.00	92.29	100.00	96.41	94.27	94.64		94.27	91.69	99.51	99.78	94.64
NEW YORK	74.89	94.97	100.00	108.27	100.02	106.08		100.02	104.06	110.57	118.34	106.08
PHILADELPHIA	77.23	106.25	100.00	95.08	97.31	94.72		97.31	92.15	92.76	98.08	94.72
CLEVELAND	87.72	102.01	100.00	101.13	104.64	102.42		104.64	99.64	104.32	96.29	102.42
RICHMOND	77.02	96.66	100.00	97.04	96.81	103.67		96.81	94.08	98.96	98.39	103.67
ATLANTA	95.78	102.00	100.00	98.55	96.56	100.31		96.56	93.36	100.82	103.27	100.31
CHICAGO	78.17	92.62	100.00	101.44	105.96	101.20		105.96	102.69	100.25	97.05	101.20
ST. LOUIS	79.23	100.10	100.00	95.83	97.95	101.93		97.95	95.66	97.21	92.63	101.93
MINNEAPOLIS	84.94	93.07	100.00	109.31	106.46	114.93		106.46	108.01	112.07	110.18	114.93
KANSAS CITY	75.95	95.63	100.00	105.27	103.95	108.79		103.95	103.23	107.49	106.44	108.79
DALLAS	92.01	101.29	100.00	96.75	96.05	100.00		96.05	99.86	98.78	92.66	100.00
SAN FRANCISCO	81.31	101.41	100.00	104.21	104.05	103.03		104.05	104.93	104.07	103.05	103.03
SYSTEM	81.46	97.97	100.00	10 19	101.49	103.25		101.49	100.58	103.77	102.93	103.25

AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	135.08	105.55	100.00	104.69	99.98	109.78		99.98	102.88	104.00	111.92	109.78
NEW YORK	116.42	98.02	100.00	102.19	100.30	101.52		100.30	103.97	102.12	102.37	101.52
PHILADELPHIA	130.27	97.06	100.00	112.14	105.47	116.45		105.47	112.85	112.27	117.99	116.45
CLEVELAND	117.33	97.17	100.00	99.58	97.36	100.70		97.36	98.80	97.53	104.63	100.70
RICHMOND	120.24	97.25	100.00	105.27	102.90	107.41		102.90	106.14	102.99	109.04	107.41
ATLANTA	101.62	94.35	100.00	107.30	104.35	111.92		104.35	107.69	105.59	111.57	111.92
CHICAGO	116.52	101.89	100.00	99.86	98.25	97.81		98.25	100.51	97.23	103.46	97.81
ST. LOUIS	129.19	98.49	100.00	99.28	98.90	95.20		98.90	99.52	96.36	102.33	95.20
MINNEAPOLIS	100.12	92.08	100.00	97.19	100.67	93.08		100.67	98.37	93.16	96.57	93.08
KANSAS CITY	121.08	100.16	100.00	97.05	97.21	95.26		97.21	97.59	94.42	98.99	95.26
DALLAS	111.04	96.17	100.00	107.54	104.88	112.54		104.88	104.50	106.29	114.48	112.54
SAN FRANCISCO	108.10	92.08	100.00	104.72	102.57	108.49		102.57	104.43	102.95	108.94	108.49
SYSTEM	114.35	97.85	100.00	102.10	100.11	103.29		100.11	102.22	100.27	105.80	103.29

OTHER CHECKS

AGGREGATE UNIT COST INDEX (SYSTEM = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	89.17	95.38	86.77	91.91	88.60	100.55	5	88.60	85.13	96.81	97.75	100.55
NEW YORK	111.89	100.45	89.67	87.80	96.62	101.38	6	96.62	88.06	80.96	85.05	101.38
PHILADELPHIA	107.45	95.44	95.13	94.84	106.94	89.74	3	106.94	90.08	100.81	81.49	89.74
CLEVELAND	110.71	139.16	118.25	131.56	131.81	130.24	11	131.81	131.48	144.34	120.24	130.24
RICHMOND	85.23	73.85	74.97	81.43	82.15	82.86	2	82.15	82.58	82.39	77.89	82.86
ATLANTA	86.58	79.26	97.66	112.25	97.25	120.27	10	97.25	114.82	120.26	115.73	120.27
CHICAGO	105.13	101.48	91.57	109.48	108.24	109.40	7	108.24	95.28	113.77	123.64	109.40
ST. LOUIS	87.88	80.31	112.49	75.02	70.30	76.53	1	70.30	69.27	77.18	83.18	76.53
MINNEAPOLIS	108.96	111.71	110.65	120.76	122.68	138.36	12	122.68	120.35	128.93	112.05	138.36
KANSAS CITY	86.98	94.91	95.06	98.42	107.01	91.48	4	107.01	98.00	95.76	93.30	91.48
DALLAS	104.69	100.99	91.40	99.97	104.60	111.18	8	104.60	97.85	102.07	96.32	111.18
SAN FRANCISCO	112.35	129.46	132.11	126.44	136.10	111.72	9	136.10	147.12	109.21	118.16	111.72

AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	87.74	101.75	100.00	108.86	101.24	138.01		101.24	85.51	124.04	135.23	138.01
NEW YORK	106.80	103.86	100.00	107.74	114.28	147.18		114.28	91.64	107.47	123.05	147.18
PHILADELPHIA	96.49	92.99	100.00	100.35	109.25	106.25		109.25	81.52	115.36	100.68	106.25
CLEVELAND	79.86	108.92	100.00	115.75	111.90	132.69		111.90	98.07	136.47	122.92	132.69
RICHMOND	96.97	91.18	100.00	112.01	109.67	126.24		109.67	96.73	121.88	124.53	126.24
ATLANTA	75.44	74.56	100.00	113.92	100.04	135.04		100.04	96.90	129.47	136.85	135.04
CHICAGO	98.07	102.72	100.00	130.18	124.04	155.35		124.04	96.08	146.35	171.72	155.35
ST. LOUIS	66.76	72.79	100.00	68.26	69.96	85.53		69.96	60.53	66.05	77.05	85.53
MINNEAPOLIS	83.29	92.96	100.00	106.92	105.11	139.47		105.11	90.41	123.27	115.66	139.47
KANSAS CITY	79.92	92.50	100.00	109.53	114.78	120.28		114.78	92.49	115.28	121.28	120.28
DALLAS	97.60	102.15	100.00	113.38	114.34	150.95		114.34	94.12	125.22	127.59	150.95
SAN FRANCISCO	72.42	90.55	100.00	98.60	99.25	90.36		99.25	94.39	92.96	109.06	90.36
SYSTEM	85.34	92.57	100.00	106.65	105.27	116.82		105.27	91.71	112.50	121.60	116.82

AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
BOSTON	104.61	100.45	100.00	91.09	90.58	78.17		90.58	112.93	81.75	79.08	78.17
NEW YORK	106.80	102.50	100.00	81.87	79.62	67.64		79.62	99.83	75.64	72.38	67.64
PHILADELPHIA	110.05	111.14	100.00	90.07	89.68	77.23		89.68	109.64	82.61	78.33	77.23
CLEVELAND	106.83	101.33	100.00	90.86	95.66	77.62		95.60	106.09	79.93	81.84	77.62
RICHMOND	103.78	101.45	100.00	89.33	90.03	79.89		90.03	104.89	83.50	78.82	79.89
ATLANTA	107.14	118.30	100.00	90.67	95.39	85.06		95.39	105.26	81.25	80.79	85.06
CHICAGO	109.65	103.41	100.00	84.19	84.57	77.13		84.57	106.15	76.06	69.98	77.13
ST. LOUIS	107.54	102.12	100.00	333.53	319.40	347.16		319.40	347.43	338.14	329.17	347.16
MINNEAPOLIS	112.53	107.64	100.00	91.66	90.68	80.75		90.68	113.58	81.79	80.60	80.75
KANSAS CITY	107.98	104.04	100.00	86.15	85.80	69.92		85.80	105.08	77.68	76.06	69.92
DALLAS	109.78	106.76	100.00	81.05	80.69	65.59		80.69	100.56	72.49	70.47	65.59
SAN FRANCISCO	106.30	104.48	100.00	96.03	94.77	83.16		94.77	112.43	89.21	87.73	83.16
SYSTEM	107.10	105.48	100.00	99.90	99.86	94.93		99.86	117.20	92.61	89.93	94.93

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

AUTOMATED CLEARING HOUSE

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	79.82	73.52	65.28	71.17	60.59	70.20	1	60.59	71.09	73.13	71.78	70.20
NEW YORK	185.11	136.50	171.59	204.84	193.49	182.07	12	193.49	200.68	222.30	195.34	182.07
PHILADELPHIA	95.80	96.47	109.89	94.69	106.87	94.42	5	106.87	97.99	82.47	94.26	94.42
CLEVELAND	104.20	106.96	102.88	92.28	96.73	94.87	6	96.73	97.90	88.79	86.72	94.87
RICHMOND	85.97	84.68	85.21	88.74	80.01	92.66	4	80.01	85.70	85.75	87.17	92.66
ATLANTA	97.29	109.40	96.38	90.18	98.20	77.88	2	98.20	92.64	88.74	85.58	77.88
CHICAGO	144.66	123.88	104.73	110.41	116.32	101.44	7	116.32	113.61	107.26	105.48	101.44
ST. LOUIS	137.27	156.48	181.67	170.09	177.71	162.66	11	177.71	167.40	168.41	167.22	162.66
MINNEAPOLIS	94.60	100.50	131.58	120.45	127.59	120.71	10	127.59	105.17	118.90	129.32	120.71
KANSAS CITY	97.60	113.95	120.22	117.09	119.10	105.30	8	119.10	120.91	115.12	113.87	105.30
DALLAS	120.88	101.42	91.35	93.38	85.02	110.02	9	85.02	86.95	94.70	105.63	110.02
SAN FRANCISCO	58.80	68.18	71.98	77.92	71.61	87.21	3	71.61	75.45	83.70	80.76	87.21
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	117.68	113.08	100.00	93.79	94.06	100.82		94.06	93.61	94.38	93.18	100.82
NEW YORK	82.21	79.87	100.00	102.70	100.93	99.48		100.93	104.54	109.15	96.53	99.48
PHILADELPHIA	84.70	88.47	100.00	74.48	87.37	80.85		87.37	76.93	63.46	73.08	80.85
CLEVELAND	98.46	104.38	100.00	77.17	84.16	86.46		84.16	81.79	72.71	71.48	86.46
RICHMOND	98.08	99.78	100.00	85.55	84.05	101.95		84.05	86.45	84.78	86.74	101.95
ATLANTA	98.13	113.97	100.00	80.42	91.21	75.67		91.21	82.63	74.07	75.30	75.67
CHICAGO	134.29	118.77	100.00	90.70	99.42	90.81		99.42	93.25	86.28	85.41	90.81
ST. LOUIS	73.45	86.48	100.00	80.54	87.56	83.94		87.56	79.20	78.10	78.05	83.94
MINNEAPOLIS	69.90	76.69	100.00	78.75	86.80	91.70		86.80	68.70	76.13	83.34	91.70
KANSAS CITY	78.93	95.17	100.00	83.79	88.60	82.12		88.60	86.46	80.68	80.32	82.12
DALLAS	127.90	110.86	100.00	87.46	82.85	112.30		82.85	81.37	86.86	97.51	112.30
SAN FRANCISCO	78.88	95.10	100.00	93.13	89.06	113.60		89.06	90.10	97.97	95.14	113.60
SYSTEM	97.21	100.40	100.00	86.03	89.51	93.76		89.51	85.96	84.25	84.79	93.76
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	58.61	76.24	100.00	124.27	115.31	138.97		115.31	121.07	126.50	134.20	138.97
NEW YORK	80.07	86.65	100.00	110.28	104.75	123.75		104.75	107.68	110.77	117.93	123.75
PHILADELPHIA	59.31	77.31	100.00	127.72	112.28	140.66		112.28	118.15	143.85	137.81	140.66
CLEVELAND	63.31	80.11	100.00	115.80	103.60	130.43		103.60	113.73	120.22	125.65	130.43
RICHMOND	53.08	73.32	100.00	128.12	118.74	131.41		118.74	124.17	129.21	140.35	131.41
ATLANTA	63.72	78.30	100.00	122.53	113.03	140.07		113.03	118.44	126.08	132.56	140.07
CHICAGO	70.41	78.22	100.00	127.02	115.52	149.68		115.52	121.61	131.25	139.70	149.68
ST. LOUIS	61.88	79.46	100.00	123.46	114.35	145.05		114.35	119.84	125.91	134.55	145.05
MINNEAPOLIS	56.21	71.48	100.00	135.22	118.52	138.64		118.52	132.23	132.37	157.75	138.64
KANSAS CITY	62.68	78.48	100.00	131.09	117.90	156.11		117.90	128.08	133.69	144.67	156.11
DALLAS	56.47	73.48	100.00	123.15	114.76	135.44		114.76	119.59	125.89	132.34	135.44
SAN FRANCISCO	60.41	78.98	100.00	121.31	116.47	129.45		116.47	120.57	119.56	128.68	129.45
SYSTEM	61.67	77.56	100.00	123.99	114.46	137.48		114.46	120.64	126.13	134.78	137.48

SUMMARY REPORT
PERFORMANCE MEASURES
FIRST QUARTER, 1985

ALL OTHER

FEDERAL RESERVE DISTRICT	1981	1982	1983	1984	1984 YTD	1985 YTD	1985 RANK	1984 I	1984 II	1984 III	1984 IV	1985 I
AGGREGATE UNIT COST INDEX (SYSTEM = 100)												
BOSTON	107.47	86.23	90.10	102.91	95.37	131.84	4	95.37	99.33	103.00	113.19	131.84
NEW YORK	56.20	56.63	66.30	69.98	65.16	62.98	1	65.16	71.13	69.50	73.82	62.98
PHILADELPHIA	161.77	203.06	249.29	193.72	199.98	210.33	12	199.98	195.14	201.07	170.84	210.33
CLEVELAND	144.56	165.75	154.25	127.37	151.43	151.05	7	151.43	123.61	158.05	97.33	151.05
RICHMOND	129.29	114.89	101.31	133.35	112.61	109.91	10	112.61	138.46	127.47	161.23	109.91
ATLANTA	108.60	100.32	80.59	74.50	74.81	68.03	2	74.81	74.32	79.27	71.41	68.03
CHICAGO	139.20	139.26	170.22	181.19	203.66	162.32	8	203.66	169.33	185.50	156.72	162.32
ST. LOUIS	180.79	179.68	133.88	116.39	118.14	110.24	3	118.14	130.20	107.46	112.27	110.24
MINNEAPOLIS	123.79	157.81	144.44	130.13	130.22	147.76	6	130.22	128.60	120.67	142.21	147.76
KANSAS CITY	180.96	222.22	158.86	162.89	158.38	178.81	9	158.38	156.59	170.84	166.00	178.81
DALLAS	237.39	154.41	137.56	112.06	100.91	135.28	5	100.91	129.84	102.84	114.20	135.28
SAN FRANCISCO	191.52	171.99	153.19	169.03	143.26	203.38	11	143.26	172.42	160.14	190.34	203.38
AGGREGATE UNIT COST INDEX (TIME SERIES 1983 = 100)												
BOSTON	117.35	106.28	100.00	99.75	100.09	118.89		100.09	90.19	101.04	107.45	118.89
NEW YORK	90.21	94.31	100.00	93.50	92.03	78.34		92.03	89.35	94.15	98.31	78.34
PHILADELPHIA	77.42	133.39	100.00	65.21	73.61	66.95		73.61	61.23	68.89	58.61	66.95
CLEVELAND	91.12	119.45	100.00	74.05	98.96	82.24		98.96	66.77	94.10	53.86	82.24
RICHMOND	124.22	125.81	100.00	112.86	103.65	152.16		103.65	105.16	109.90	133.78	152.16
ATLANTA	92.60	115.21	100.00	87.20	97.90	69.79		97.90	82.21	91.37	80.06	69.79
CHICAGO	83.00	98.38	100.00	92.57	114.51	77.55		114.51	81.11	95.20	79.35	77.55
ST. LOUIS	128.92	140.19	100.00	80.67	90.00	72.19		90.00	83.55	76.38	74.87	72.19
MINNEAPOLIS	86.85	116.26	100.00	79.73	87.43	87.17		87.43	72.82	74.78	85.29	87.17
KANSAS CITY	112.71	149.99	100.00	91.95	98.15	93.60		98.15	83.10	97.24	90.47	93.60
DALLAS	179.54	121.38	100.00	74.77	73.75	85.29		73.75	81.37	70.07	74.98	85.29
SAN FRANCISCO	138.26	126.40	100.00	95.06	84.75	107.50		84.75	91.15	98.93	113.61	107.50
SYSTEM	106.40	110.69	100.00	87.35	94.55	81.71		94.55	81.77	88.43	85.57	81.71
AGGREGATE VOLUME INDEX (TIME SERIES 1983 = 100)												
BOSTON	91.10	90.69	100.00	118.38	106.91	122.12		106.91	120.26	121.99	124.36	122.12
NEW YORK	106.37	102.63	100.00	109.77	101.54	124.20		101.54	113.04	110.27	114.22	124.20
PHILADELPHIA	181.97	94.93	100.00	121.42	107.36	134.08		107.36	126.59	123.19	128.54	134.08
CLEVELAND	122.18	90.64	100.00	144.32	111.33	126.48		111.33	163.80	112.27	109.90	126.48
RICHMOND	93.28	97.65	100.00	97.64	98.32	95.53		98.32	101.45	96.54	94.23	95.53
ATLANTA	93.91	79.35	100.00	127.79	111.48	158.00		111.48	136.19	121.08	142.42	158.00
CHICAGO	137.48	105.29	100.00	96.13	101.80	99.51		101.80	99.90	83.89	98.94	99.51
ST. LOUIS	121.81	90.74	100.00	181.71	128.31	162.70		128.31	135.89	152.20	150.45	162.70
MINNEAPOLIS	170.01	107.88	100.00	136.17	118.16	158.04		118.16	141.32	144.57	140.62	158.04
KANSAS CITY	127.42	97.55	100.00	100.99	94.81	103.99		94.81	106.79	97.02	105.36	103.99
DALLAS	97.17	99.25	100.00	140.31	128.01	163.49		128.01	127.45	157.15	148.63	163.49
SAN FRANCISCO	95.38	94.96	100.00	120.43	119.64	128.60		119.64	120.26	122.66	139.14	128.60
SYSTEM	107.27	96.88	100.00	116.58	107.01	128.19		107.01	120.86	114.41	124.03	128.19

Appendix D

FEDERAL RESERVE EXPENDITURES, EMPLOYMENT AND PRODUCTIVITY

Overview

Over the 1974-1984 period as a whole Federal Reserve System expenditures grew at an average annual rate of 0.7 percent in real terms[1] and employment declined by 3671, or 13 percent. Table 1 indicates important variations in the rate of spending growth over time. For example, the 1974 to 1979 period was characterized by improved productivity in many of the operating functions at the Reserve Banks and by a multi-year cost control program at the Board and the Reserve Banks. In real terms, costs actually declined from 1977 through 1979. However, the implementation of the Monetary Control Act in 1980 resulted in significant transitional costs in the monetary and economic policy area and increased expenditures in Supervision and Regulation. The Act also had a profound impact on the Federal Reserve's role as a service provider, since it required the System to explicitly price the services it provides to depository institutions rather than to supply them without explicit charge, and also permitted nonmember institutions access to Federal Reserve services.

At the beginning of 1984, the System adopted contemporaneous reserve requirements, further increasing expenses in data reporting--which comprises 40 percent of all expenditures in Monetary and Economic Policy.

Note: Throughout this document, real dollars are on the basis of GNP implicit price deflator (1972 = 100).

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[1] Reserve Bank and Board expenses exclude the cost of currency because the Fed reimburses the Bureau of Printing and Engraving for their total costs of producing Federal Reserve notes. See Table 1.

Table 1
Total System Expenses in Actual and Constant Dollars[1]
(dollars in millions)

Year	Reserve Banks[2]		Board[3]		Banks + Board		Percentage Change	FR Currency		Total System		Percentage Change
	Expenses	Real $	Expenses	Real $	Expenses	Real $	Real $	Expenses	Real $	Expenses	Real $	Real $
1974	519.0	450.9	31.6	27.4	550.6	478.4		30.2	26.2	580.8	504.6	
1975	562.1	447.2	36.0	28.6	598.1	475.8	-0.5	37.2	29.6	635.2	505.3	0.1
1976	609.6	460.8	40.4	30.5	650.0	491.3	3.3	48.8	36.9	698.8	528.2	4.5
1977	626.9	447.8	45.6	32.6	672.5	480.4	-2.2	55.0	39.3	727.5	519.6	-1.6
1978	654.6	435.2	49.5	32.9	704.1	468.1	-2.5	60.1	39.9	763.2	507.4	-2.3
1979	693.9	424.7	53.9	32.9	747.8	457.6	-2.2	68.4	41.9	816.2	499.5	-1.6
1980	792.8	444.4	60.4	33.9	853.2	478.2	4.5	73.1	41.0	926.3	519.2	3.9
1981	886.1	453.0	62.4	31.9	948.5	484.9	1.4	82.9	42.4	1031.4	527.3	1.5
1982	973.6	469.4	67.9	32.7	1041.5	502.2	3.5	98.4	47.4	1139.9	549.6	4.2
1983	1028.5	477.7	72.2	33.5	1100.7	511.2	1.8	152.1[4]	70.6[4]	1252.8[4]	581.9[4]	5.9[4]
1984	1067.8	478.0	77.9	34.9	1145.7	512.8	0.3	162.6	72.8	1308.3	585.6	0.6
Avg. Annual Growth	7.5%	.6%	9.4%	2.4%	7.6%	.7%		18.3%	10.7%	8.5%	1.5%	

1/ Data for Reserve Banks and the Board of Governors are not collected through the same accounting system. Total System expenses are defined as Reserve Bank expenses, including depreciation, Board of Governors' operating expenses and estimated depreciation, and FR currency expenses. Constant dollar data is deflated by GNP Implicit Price Deflator 1972=100.

2/ Any differences between total expenses as reported in the Board's Annual Report and total expenses as shown on this table are due to the exclusion of cost of earnings credits in PACS reports and other minor timing adjustments.

3/ Any differences between expenses as reported in the Board's Annual Report and expenses shown on this table are due to netting of minor receipts against expenses for performance reporting compared to the Annual Report which reveals gross receipts and expenditures. Also, the Board's current budgeting and accounting procedures do not recognize a capital items category. All items purchased are expensed in the year they are received. Since this can distort the trend in operating expenses when large capital items (buildings and computers) are involved, the Board's operating budget shows these items separate from operating expenses. In the treatment here, an estimated depreciation schedule was developed covering the Board's large capital items over the previous decade. The large items depreciated in the estimate include costs for the Martin Building, for renovating the Eccles Building, and purchases of computer systems and upgrades.

4/ As a result of an accounting change in 1983, $30,442,000 of prior year currency expenses were recognized in 1983. Also, 1983 F.R. currency costs include the full cost of $30 million of equipment purchased by the Bureau of Engraving and Printing in 1983. This equipment is expected to benefit the Federal Reserve over future periods. Excluding the full one-time impact of the accounting change and apportioning the cost of currency printing equipments over the future years of benefit would reduce 1983 currency costs to $94,693,000 and total System expenses to $1.195 billion, respectively.

The System employment trend mainly reflects developments at the Reserve Banks since Bank employment makes up 94 percent of System employment. As shown in Table 2, employment declined for five years after 1974, when a total of 3,377 employees or 12.1 percent of total employment were cut from the payroll. In 1980 and 1981, employment increased 2.6 percent and 1.1 percent, respectively, largely as a result of the Monetary Control Act, but in 1982 and 1983 employment again declined, reflecting cutbacks in response to significant volume losses, largely in check processing.

Table 2
Total System Employment

Year	Reserve Bank[1]	Board of Governors[2]	Total System	Percent Change
1974	26,567	1,361	27,928	6.6
1975	26,341	1,443	27,784	-0.5
1976	25,186	1,446	26,632	-4.2
1977	24,300	1,473	25,773	-3.2
1978	23,479	1,469	24,948	-3.2
1979	23,104	1,447	24,551	-1.6
1980	23,682	1,516	25,198	2.6
1981	23,989	1,491	25,480	1.1
1982	23,230	1,525	24,755	-2.9
1983	22,883	1,583	24,466	-1.2
1984	22,669	1,588	24,257	-0.9
Avg. Annual Growth Rate	-1.6%	1.6%	-1.4%	

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[1] Average number employees and officers as reported in the Functional Expense Accounting System from 1973-1976, and in the PACS system from 1977-1983.

[2] Employees at year-end.

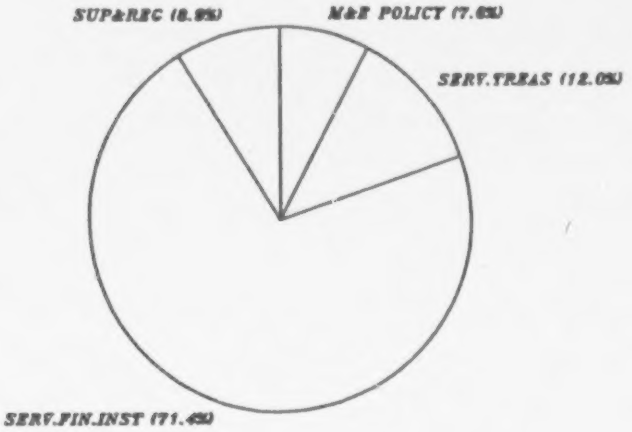
Total Federal Reserve spending comprises three broad categories: expenditures by the Board of Governors, expenditures by the Reserve Banks, and the purchase of Federal Reserve currency. Reserve Banks account for about 84 percent of total spending outlays, Board expenses for about 7 percent and Federal Reserve currency for 9 percent on average for the 1974 to 1984 period. For analytical purposes, the Federal Reserve usually evaluates Reserve Bank expenditures minus currency costs, since the Reserve Banks reimburse the Bureau of Engraving and Printing for its total production costs.

Figure 1 shows the distribution of Federal Reserve expenditures by major service line in 1977 compared to 1984. The year 1977 is used as the base period since it is the first year for which PACS data on expenditures by service line are available. The most notable change is the decline in the share of expenses for services to financial institutions and the public, from approximately 70 percent of the total in 1977 to about 60 percent in 1984. Following the MCA, the priced services component of Federal Reserve activities declined from an estimated one-half of total Federal Reserve spending to approximately 40 percent. This decline in the share of services to financial institutions and the public was offset by increases in the shares of Monetary and Economic Policy and Supervision and Regulation.

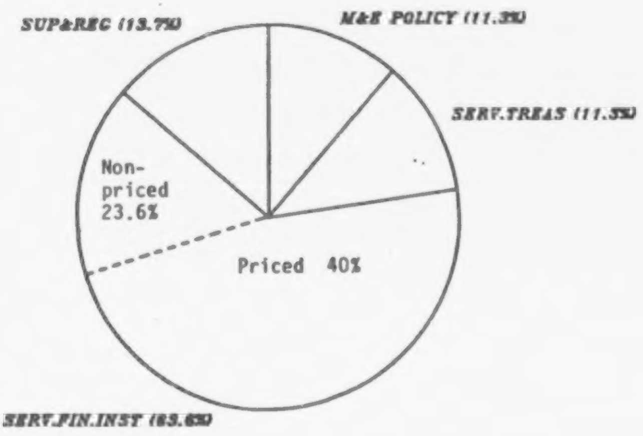
Figure 1

SYSTEM EXPENSES BY MAJOR PROGRAM

1977



1984



Note: System policy and Board support, which accounts for approximately 2.3% of total expenses, has been allocated by expense. PACS data are not available for the Board of Governors so its cost distribution has been estimated.

I. Total System Expenses and Employment by Program

The data given in this section for System Functions include both expenses incurred at the Reserve Banks and at the Board of Governors. The data are derived from two separate accounting systems. The Reserve Bank portion of the combined System data includes all direct costs as well as fully allocated support and overhead costs. The Board of Governors portion of the System cost includes direct plus data processing costs. Expenses for "System Policy Direction and Board Support," and estimated capital depreciation have been distributed into the four major service lines used by the Reserve Banks.

A. Monetary and Economic Policy

Expenditures in monetary and economic policy had the second fastest rate of increase over the last seven years, growing at an average annual rate of 6.6 percent in real terms. As Figure 2 indicates, the bulk of this increase occurred from 1981 to 1983. Approximately 40 percent of direct activity costs in this area are for data collection and preparation. In large part the growth in monetary and economic policy spending was a result of an increase in the number of institutions reporting deposit data and reserve requirements from about 5,500 before passage of the MCA to more than 17,000 afterwards. This increase improved the System's ability to measure changes in the monetary aggregates. Expenditures on Monetary and Economic Policy began to moderate in 1982. More than half of the relatively small increase for 1983 was attributable to the cost of implementing contemporaneous reserve requirements, a change made to improve monetary control. In 1984 expenditures declined slightly.

Figure 2

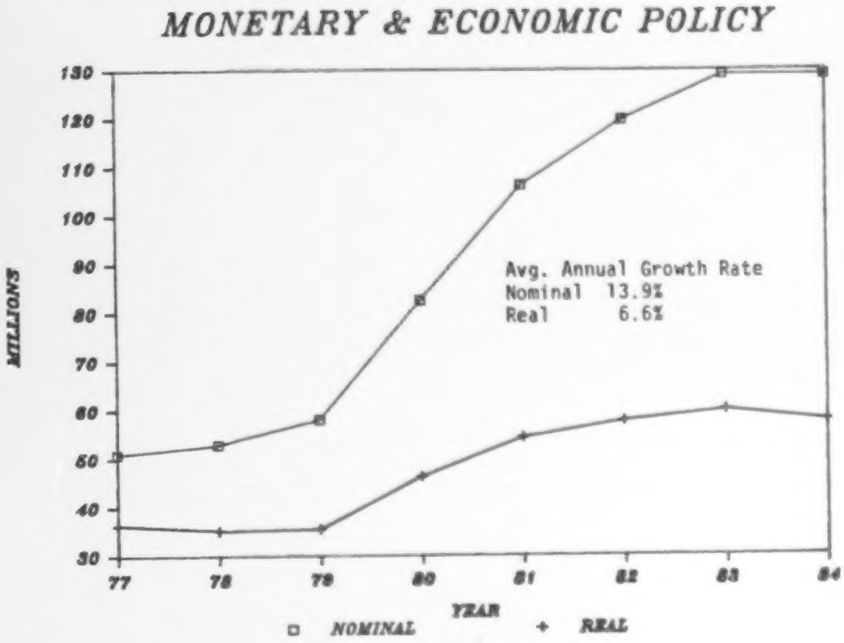


Table 3
Monetary and Economic Policy
System Expenses and Employment 1977-1984
(dollars in millions)

Year	Total Expense	Percent Change	Expenses Constant Dollars	Percent Change Constant Dollars	Total Employees	Percent Change
1977	$52.30		$37.36		1,220	
1978	54.50	4.2	36.14	-3.3	1,184	-3.0
1979	59.70	9.5	36.54	1.1	1,180	-0.3
1980	84.20	41.0	47.20	29.2	1,247	5.7
1981	108.10	28.4	55.27	17.1	1,335	7.1
1982	121.50	12.4	58.58	6.0	1,360	1.9
1983	130.90	7.7	60.80	3.8	1,414	4.0
1984	130.20	-0.5	58.28	-4.1	1,417	0.2
Avg. Annual Growth Rate		13.9		6.6		2.2

B. Services to the Treasury and Government Agencies

One of the responsibilities Congress gave the Federal Reserve was to act as fiscal agent for the U.S. Government. In this role the Federal Reserve provides a number of services to the Treasury and other government agencies. For example, the Federal Reserve issues and redeems Treasury and some other government agency securities. Through their electronic book entry system, the Reserve Banks also maintain bookkeeping records for government securities. In addition, a number of other services are provided, such as redeeming and destroying food stamps for the Department of Agriculture. As Figure 3 indicates, over the last seven years significant year-to-year changes took place in expenditures; to some extent this is a result of fluctuations in the purchases of Treasury securities by the public, and procedural changes requested by the Treasury. Over the period as a whole, expenditures in real dollars were flat. Employment fell by 206 or 10.3 percent between 1977 and 1984.

Figure 3

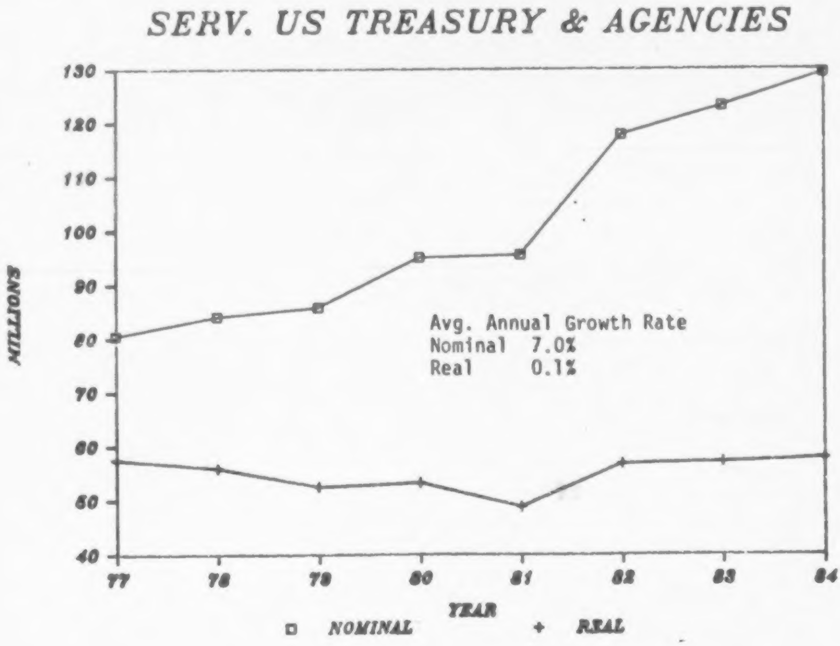


Table 4
Services to U.S. Treasury and Government Agencies
System Expenses and Employment
1977-1984
(dollars in millions)

Year	Total Expense	Percent Change	Expenses Constant Dollars	Percent Change Constant Dollars	Total Employees	Percent Change
1977	$80.6		$57.6		2,004	
1978	84.2	4.5	55.8	-3.0	1,919	-4.2
1979	85.9	2.0	52.6	-5.9	1,883	-1.9
1980	95.1	10.7	53.3	1.4	1,946	3.3
1981	95.6	0.5	48.9	8.3	1,881	-3.3
1982	117.9	24.0	56.9	16.3	1,851	-1.6
1983	123.2	4.5	57.2	0.7	1,839	-0.6
1984	129.4	5.4	57.9	1.2	1,798	-2.2
Avg. Annual Growth Rate		7.0		0.1		-1.5

C. Services to Financial Institutions and the Public

Prior to passage of the MCA about 5,000 banks, mostly larger institutions, were eligible for Federal Reserve services. More than 7,700 depository institutions now use Federal Reserve services. The objectives of the pricing provisions of the Monetary Control Act were to improve efficiency in the payments system through enhanced competition, while assuring that an adequate level of payment services was available nationwide. The Act also required that over the long run, fees for priced services be established on the basis of all direct and indirect costs actually incurred in providing the services, including the cost of float and an allocation of imputed costs (taxes and the cost of capital) that would have been incurred had the services been furnished by a private business firm. The latter comprises what is known as the Private Sector Adjustment Factor, or the PSAF.[2]

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[2] Board of Governors of the Federal Reserve System, *The Federal Reserve System - Purposes and Functions*, Washington, D.C. 1984, p. 104.

Beginning in 1981 and throughout 1982 the Reserve Banks experienced a significant decline in the demand for some of their services, and for commercial check processing in particular. The initial result was that Federal Reserve expenditures on priced services were greater than the income generated by fees.

The Reserve Banks began to make resource adjustments to reduce costs almost immediately. For example, total employment in this service line declined 1.4 percent in 1981 and 9.5 percent in 1982. In commercial checks alone, employment declined by 833. "Fixed cost" adjustments took longer to make but by 1983 they were well underway. Prices were also changed to increase revenues. Beginning in 1983 an imputed cost for Federal Reserve float[3] was also included as a component of total costs. By 1984 the market test of pricing required by the Monetary Control Act was being met, and all costs including float and the PSAF were fully recovered. As Figure 4 indicates, total expenditures in this area, including priced and nonpriced services, decreased in real terms at an annual average rate of 0.7 percent between 1977 and 1984.

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[3] Float, which occurs primarily in the process of collecting commercial checks, is created when the Federal Reserve credits a payee institution for its collections before it debits the account of the payor institution. In effect, float is an interest-free loan from the Federal Reserve. Prior to 1983 float was not priced but was instead reduced through operational improvements. Starting in 1983 the cost of float calculated on the basis of the federal funds rate has been included in Federal Reserve prices.

Figure 4

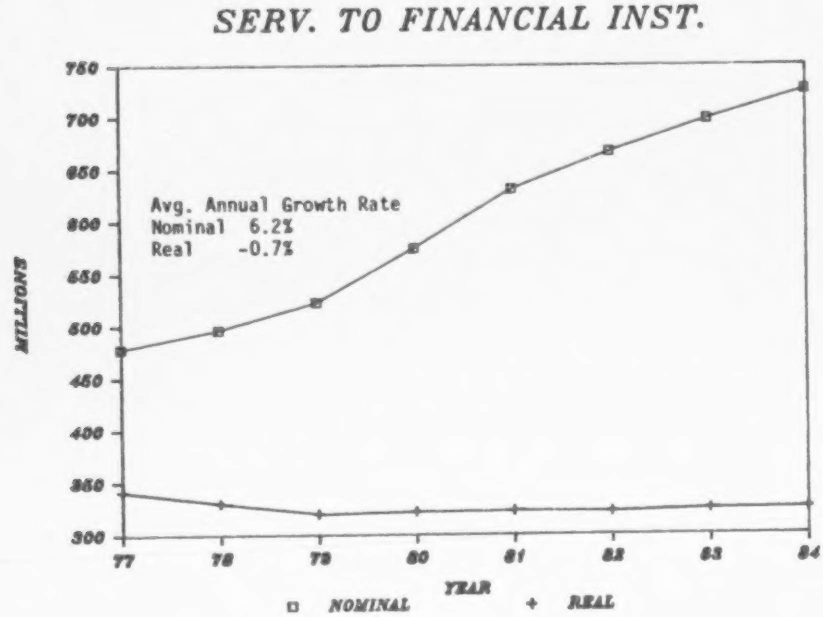


Table 5
Services to Financial Institutions and the Public
System Expenses and Employment
1977-1984
(dollars in millions)

Year	Total Expense	Percent Change	Expenses Constant Dollars	Percent Change Constant Dollars	Total Employees	Percent Change
1977	$479.20		$342.29		10,355	
1978	497.40	3.8	329.84	-3.6	9,958	-3.8
1979	523.90	5.3	320.62	-2.8	9,894	-0.6
1980	575.50	9.9	322.59	0.6	9,731	-1.7
1981	632.30	9.9	323.26	0.2	9,591	-1.4
1982	668.30	5.7	322.23	-0.3	8,682	-9.5
1983	699.30	4.6	324.80	0.8	8,559	-1.4
1984	728.20	4.1	325.96	0.4	8,535	-0.3
Avg. Annual Growth Rate		6.2		-0.7		-2.7

D. Supervision and Regulation

Supervision and regulation was the fastest growing area of Federal Reserve expenditures over the last seven years, increasing by an average annual rate of 7.4 percent in real terms. (See Figure 5.) Much of this rise was accounted for by an increased workload. For example, the number of bank holding company inspections rose at an average annual rate of 17.4 percent over the period. Similarly, the number of bank holding company applications per year more than doubled, as did the number of financial institutions monitored. The number of cease and desist orders issued per year tripled.

To some extent this increase in workload reflects the increase in bank holding company formations, the accelerating pace of change in the financial sector following elimination of interest rate ceilings on deposits, and deregulation in general. The MCA also contributed to the increase in spending on Supervision and Regulation through an increase in monitoring Reserve accounts. Additionally, legislation such as the International Banking Act, the Community Reinvestment Act, and the Financial Institutions Regulatory and Interest Rate Control Act also increased the Federal Reserve's responsibilities.

Figure 5

SUPERVISION & REGULATION

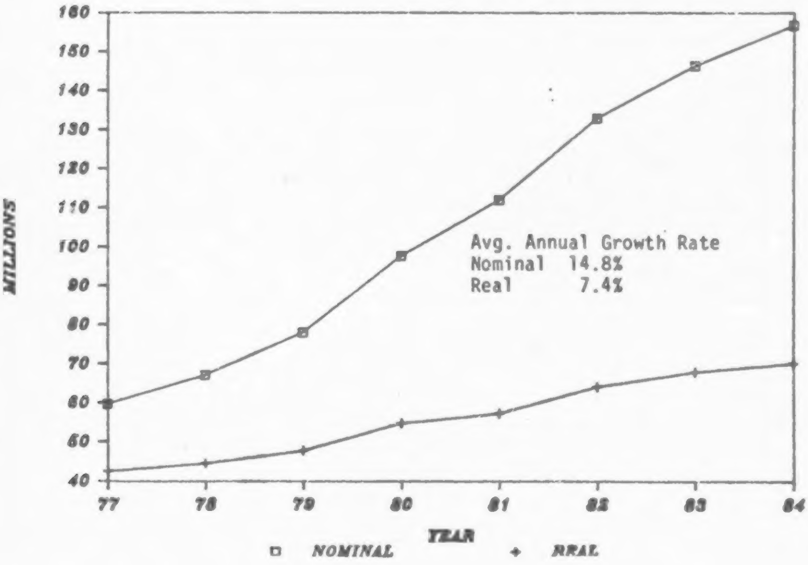


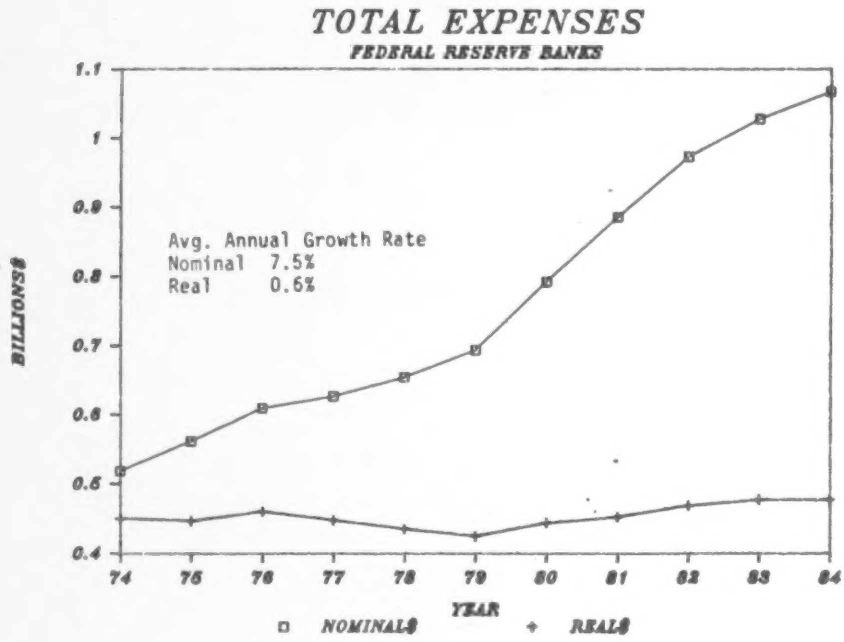
Table 6
Supervision and Regulation
System Expenses and Employment
1977-1984
(dollars in millions)

Year	Total Expense	Percent Change	Expenses Constant Dollars	Percent Change Constant Dollars	Total Employees	Percent Change
1977	$60.20		$43.00		1,501	
1978	67.70	12.5	44.89	4.4	1,579	5.2
1979	78.60	16.1	48.10	7.2	1,668	5.6
1980	98.30	25.1	55.10	14.6	1,856	11.3
1981	112.70	14.7	57.62	4.6	2,001	7.8
1982	133.70	18.6	64.46	11.9	2,069	3.4
1983	147.20	10.1	68.32	6.0	2,152	4.0
1984	158.10	7.4	70.77	3.6	2,186	1.6
Avg. Annual Growth Rate		14.8		7.4		5.5

II. Reserve Bank Expenses and Employment

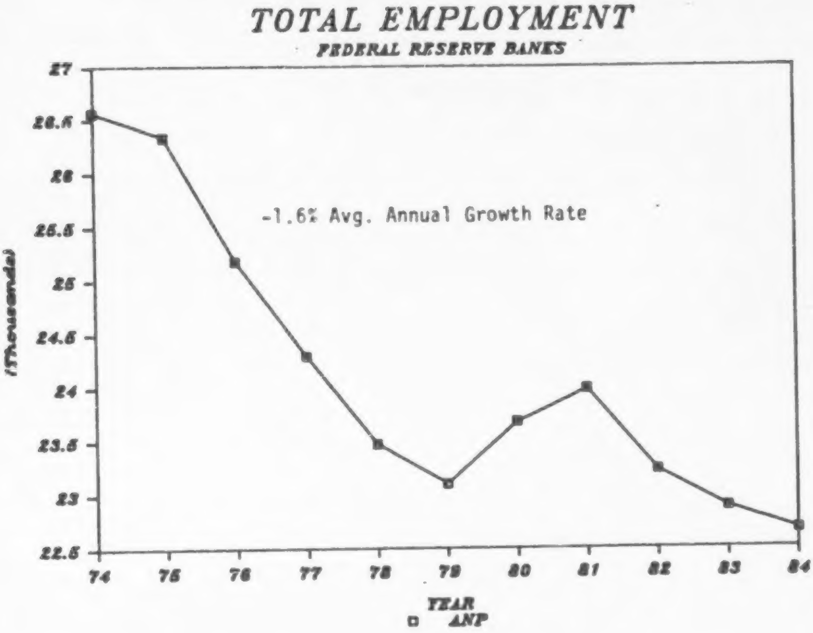
Reserve Bank expenses (excluding currency) show an average annual growth of 7.5 percent (0.6 percent in constant dollars), while employment decreased at an average annual rate of 1.6 percent. However, as indicated by Figures 6 and 7, significant changes in expenses and employment took place at the same time.

Figure 6



Note: These data are derived from PACS' highly detailed accounting and management information system. It is important to point out that the PACS reports themselves are much more disaggregated. Data on spending are published quarterly at each Reserve Bank office, by a number of subservice lines and by object of expenditure. These data are available to the public.

Figure 7



In the early seventies, the Reserve Banks carried out a systemwide program to improve the nation's payment mechanism system by establishing Regional Check Processing Centers (RCPCs) to achieve more timely check clearing. While most RCPCs were in house, a major shift from daytime operations to nighttime operations took place. In addition, 11 offsite RCPCs were organized and staffed. The improved timeliness and service the RCPCs offered brought in additional volume. With their establishment, there was a determined effort to make efficiency and productivity gains by using improved automated equipment and emphasizing cost restraint. Employment at Reserve Banks was reduced by 3,463 or 13.0 percent (from 26,567 in 1974 to 23,104 in 1979) and expenses, in constant dollars, decreased over the period from $451 million in 1974 to $425 million in 1979, an average annual decline of 1.2 percent. These reductions were made in spite of continued expansion in volumes processed. (Volume growth in check processing, the largest operating area, averaged 6.8 percent per year over this same period.) When the Monetary Control Act (MCA) was passed in 1980, virtually no resources at the Banks could be redirected to accomplish the new requirements placed on the System by the Act. Resources had to be expanded, which reversed the trend in expenses and employment in place since 1974.

Adjusting to the requirements of the MCA is clearly the most important factor affecting Reserve Bank operations. Previously, reserve requirements had been imposed only on member banks. The new legislation, however, resulted in a great increase in the number of depository institutions reporting deposit data and maintaining reserve accounts at the Reserve Banks.

Another feature of the MCA which had a major impact on Reserve Bank resources, was the requirement that the Federal Reserve price explicitly certain services provided to depository institutions. Heretofore, these services were provided to member banks at no explicit cost. Thus, the Reserve Banks had to establish new operations for pricing, billing, and customer servicing in response to passage of the MCA.

MCA requirements led to an increase of 578 staff members in 1980, reversing a five-year period of decline. In the following year an additional 307 staff were added bringing Reserve Bank employment to 23,989. This level was still 2,578 or 9.7 percent below the 1974 staff level of 26,567. However, as pricing resulted in volume loss, the Reserve banks adjusted rapidly. Staff was reduced throughout 1982 (by 759) and during 1983 (by 347). The 1984 Reserve Bank staff level of 22,669 was the lowest in the decade.

The trend in expenses also shows the impact of the MCA. Expenses increased 14.3 percent in 1980, the largest annual increase since 1974. (Adjusted for inflation the increase was 4.5 percent, also the highest since 1974.) Year-over-year increases have been lower since 1980; 11.8 percent for 1981 over 1980 (2.3 percent adjusted for inflation); 9.9 percent for 1982 (3.6 percent adjusted for inflation); and 5.6 percent for 1983 (1.3 percent adjusted for inflation), and 3.8 percent for 1984 (0.1 percent adjusted for inflation).

Reserve Bank Expenses and Employment by Service Line

Tables 7 and 8 show Reserve Bank expenses and employment by PACS service lines from 1977 through 1984. Although numerous accounting changes took place over this six-year period, the general trends are captured in the statistics. For example, Reserve Bank expenses and employment have grown more rapidly in monetary and economic policy (16.4 percent and 3.7 percent average annual growth rate (AAGR), respectively) and supervision and regulation (15.1 percent and 5.8 percent AAGR, respectively) than in other areas during this period.

Table 7
Federal Reserve Bank Expenses by PACS Service Line
1977-1984
(dollars in thousands)

Year	Monetary and Economic Policy	Services to the U.S. Treasury & Gov't. Agencies	Svcs. to[1] Financial Institutions & the Public	Supervision and Regulation of Banks	Total
1977	$34,247	$78,569	$461,366	$52,698	$626,881
1978	34,876	82,072	479,353	58,291	654,592
1979	38,244	83,536	504,371	67,754	693,904
1980	59,567	92,486	554,686	86,068	792,804
1981	81,163	93,401	611,698	99,863	886,125
1982	93,010	115,126	646,151	119,316	973,603
1983	100,443	120,256	675,918	131,848	1,028,465
1984	99,351	126,307	701,453	140,690	1,067,802
Avg. Annual Growth Rate	16.4%	7.0%	6.2%	15.1%	7.9%
Constant Dollars[2]	8.9%	0.1%	-0.7%	7.6%	0.9%

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[1] Excludes FR currency costs. See page 1.

[2] GNP Deflator 1972=100.

Table 8
Federal Reserve Bank Employment by PACS Service Line
1977-1984

Year	Monetary and Economic Policy	Services to the U.S. Treasury & Gov't. Agencies	Services to Financial Institutions & the Public	Supervision . and Regulation	Support	Overhead
1977	641	2,004	10,246	1,273	4,292	5,858
1978	610	1,919	9,850	1,337	4,146	5,616
1979	597	1,883	9,790	1,411	4,055	5,367
1980	618	1,946	9,614	1,589	4,238	5,680
1981	717	1,881	9,480	1,733	4,434	5,745
1982	743	1,851	8,566	1,796	4,599	5,676
1983	804	1,838	8,424	1,862	4,367	5,589
1984	826	1,798	8,395	1,885	4,340	5,424
Actual	185	-206	-1,851	612	48	-434
% Change	29%	-10.3%	-18.1%	48%	1.1%	-7.4%
Avg. Annual Growth Rate	3.7%	-1.5%	-2.8%	5.8%	.2%	-1.1%

A. Service Line I - Monetary and Economic Policy. The PACS accounting system captures in service line I all costs associated with determining and achieving the monetary policy of the System. Table 9 depicts expenses and employment from 1977 to 1984. Expenses are broken out by cost of activities (all direct costs including data processing and occupancy costs), System projects (major systemwide development efforts), and overhead cost allocations, such as administration, personnel, accounting, etc. Employment data are for direct activities only since support and overhead employment are not allocated to output areas.

Table 9
Monetary and Economic Policy (Service Line I)
Expenses and Employment All Reserve Banks
(dollars in thousands)

	Expenses					Employment	
Year	Cost of Activities	System Projects	Overhead	Total	% Change	Employees	% Change
1977	$23,662	$ 67	$10,518	$34,247		641	
1978	24,894	32	9,950	34,876	1.8%	610	-4.8%
1979	26,380	112	11,752	38,244	9.7	598	-2.0
1980	29,214	16,580	13,768	59,567	55.7	618	3.4
1981	36,093	29,108	15,962	81,163	36.3	717	16.2
1982	45,492	20,851	26,677	93,010	14.6	743	3.6
1983	51,185	21,194	28,064	100,443	8.0	804	8.2
1984	55,055	13,975	30,320	99,351	-1.1	826	2.7
Avg. Ann. Growth Rate	12.8%	114.5%	16.3%	16.4%		3.7%	
Constant Dollars	5.6%	100.7%	8.9%	8.9%			

Note: Support and overhead costs have been allocated into the four output service lines.

From 1977 to 1984, expenses in monetary and economic policy increased 16.4 percent on an average annual basis, (8.9 percent in constant dollars) and employment increased by 3.7 percent. In 1978, total employment declined by 31 or 4.8 percent, and in 1979, total employment declined by 13 or 2.1 percent. Beginning in 1980 and continuing throughout 1983, however, expenses and employment grew substantially in monetary and economic policy for numerous reasons. Large expense increases occurred in System project and overhead areas, and in the data reporting area.

System Projects

A System project cost increase of $21.1 million from 1977 to 1983 occurred between 1979 and 1983. This increase results directly from the passage of the Monetary Control Act of 1980 (MCA). All costs of meeting MCA requirements were accumulated in a System project and allocated to this service line. Following are the actual costs of implementing the MCA:

Table 10
MCA System Project
1980-1983

Year	Amount
1980	$16,459,690
1981	28,122,193
1982	14,562,922
1983	5,646,490
TOTAL	$64,791,295

Other System projects related to the System's long-range automation program were allocated to this service line during this period. Also, since 1982 the cost of moving toward contemporaneous reserve requirements (CRR) was allocated entirely to this service line. Following are the costs of implementing CRR:

Table 11
CRR System Project
1982-1984

Year	Amount
1982	$ 89,613
1983	6,499,389
1984	5,708,901

Overhead

A sharp increase in overhead allocations occurred in 1982 when costs increased $10.7 million or 67.1 percent. This increase resulted primarily from a thorough review of the PACS accounting system methods for allocating overhead. The review was conducted in order to achieve overhead allocations which would associate costs more closely with benefits. For example, beginning in 1982, cost of the Research Library at Reserve Banks was allocated entirely to service line I - monetary and economic policy, whereas before 1982, these costs were spread to all services on a ratio basis.

Data Reporting

As discussed previously, expenses of statistical reporting to the Board grew at an average annual rate of 18.1 percent from 1977 to 1984.

The cost of data reporting increased sharply in 1980, and is attributed to several pieces of legislation which affected the volume and complexity of data reports.

- The Depository Institutions Deregulation and Monetary Control Act of 1980 (MCA), which applied Federal Reserve requirements to all U.S. depository institutions with certain types of accounts, greatly increased the number of depository institutions reporting monetary aggregates data to and maintaining reserve accounts with the Federal Reserve.

- The International Banking Act of 1978 (IBA) created an increased need for supervisory, regulatory, and financial information and resulted in large increases in the number of respondent institutions reporting deposits and financial data. In 1980, previous reporting instruments were replaced with the far more detailed quarterly Report of Assets and Liabilities of U.S. Branches and Agencies of Foreign Banks, and the quarterly Report of Condition for Edge Act Corporations.
- In 1981, the Board of Governors' authorization of International Banking Facilities (IBFs) resulted in the implementation of a number of new statistical reports on IBF activities designed to monitor IBFs and to interpret changes in the monetary aggregates. In addition, IBFs reporting on the Treasury International Capital series, which the Federal Reserve handles on behalf of the U.S. Treasury, have increased greatly.
- Passage of the Garn-St Germain Act of 1982, and related actions by the Depository Institutions Deregulation Committee (DIDC), led to the deregulation of deposit accounts, reporting changes and significant workload increases associated with the monetary aggregates data flows.
- And finally, the change from lagged to Contemporaneous Reserve Requirements (CRR), which was implemented on February 2, 1984, resulted in significant preparatory system development costs in 1983, and on a continuing basis has resulted in an increased workload associated with the required additional monitoring of reserve calculations and reserve position performance, the processing of reserve statements, as well as the added complexity of the monetary aggregates data flows. These amounts are direct results of volume increases pursuant to mandate and changes in reserve administration.

In interpreting these increases, it must be recognized that the workload associated with the volume increases is not strictly additive. The need to assure data quality, which includes comparisons between multiple report series filed by the same institutions, requires that each additional piece of information be run against other data reported by the institution. Therefore, overall workload and costs are expanded to a greater degree than would have been the case for simple collection of the additional data.

B. Service Line II - Services to the U.S. Treasury and Government Agencies.

Service line II in the PACS system includes Reserve Bank costs for acting as fiscal agent for the U.S. government as well as performing other operations for governmental agencies. Examples include issuing, servicing and redeeming savings bonds and other instruments of public debt; processing government agency coupons; processing food coupons; performing Treasury tax and loan accounting; and maintaining the Treasury's general account. Workloads are largely determined by policies of the governmental agencies involved.

As shown on Table 12, from 1977 to 1984, expenses in services to the Treasury and government agencies grew at an average annual rate of 7.0 percent and 0.1 percent in constant dollars. Employment declined by 206 or -10.3 percent. On an average annual basis, employment declined by 1.5 percent.

Table 12
Services to the U.S. Treasury and Government Agencies (Service Line II)
Expenses and Employment All Reserve Banks
(dollars in thousands)

	Expenses					Employment	
Year	Cost of Activities	System Projects	Overhead	Total	Percent Change	Employees	Percent Change
1977	$51,751	$ 555	$26,263	$78,569		2,004	
1978	55,197	355	26,520	82,072	4.5%	1,919	-4.2%
1979	54,644	925	27,966	83,536	1.8	1,883	-1.9
1980	58,933	2,133	31,420	92,486	10.7	1,946	3.3
1981	60,472	2,092	30,837	93,401	1.0	1,881	-3.3
1982	66,898	6,152	42,076	115,126	23.3	1,851	-1.6
1983	71,083	6,908	42,265	120,256	4.5	1,839	-0.6
1984	76,083	7,014	43,210	126,307	5.0	1,798	-2.2
Avg. Annual Growth Rate	5.7%	43.7%	7.4%	7.0%		-1.5%	
Constant Dollars	-1.1%	34.4%	.5%	.1%			

In the late 1970s the volume increase was due primarily to high interest rates. The rapid increase in workloads in the fiscal agency forced many Reserve Banks to increase staff in the short term and undertake automation efforts for the long term. A long-term automation development effort to standardize the securities transfer and safekeeping systems (SHARE) among the Reserve Banks also began in 1980. Table 13 below shows the costs of this program from 1980 to 1984. This development effort has been primarily included in service line II.

Table 13
SHARE Costs
1980-1984 (in thousands)

Year	Amount
1980	$2,381
1981	1,448
1982	626
1983	1,670
1984	3,881

Treasury changes in the savings bond program also increased workload levels and complexity in 1980. These changes involved the introduction of a new series of savings bonds and the accelerated remittance of savings bond sales. The Reserve Banks, as fiscal agents, were required to increase the level of accounting detail, process more frequent remittances from issuing agents and operate under additional, more complex savings bond issuing procedures. The changes also required the recall, reconcilement, and exchange of unissued series of savings bond stock from over 40,000 issuing agents. As a result, the Reserve Banks found it necessary to increase staff in this area in 1980 and undertake automation efforts.

In 1981 a general decline in Treasury volume of 11.4 percent resulted in Reserve Banks reducing employment by 3.3 percent in this area and holding expenses flat (1.0 percent increase). The dramatic drop in volume caused unit costs to increase by 12.2 percent even though expenses increased only 1.0 percent. The decline in volume occurred mainly in the marketable security area where volume dropped by 34.9 percent. Volume also declined in the savings bond area by 5.9 percent.

In 1982, expenses increased by 23.3 percent, employment and volume continued to decline (1.6 percent and 6.2 percent, respectively), and unit costs increased by 32.5 percent.

Of the 23.3 percent or $21.7 million increase, direct and support costs rose only 10.6 percent; however, System project and overhead costs increased 46.5 percent. A fundamental reevaluation of several System project and overhead allocations in 1981 associated overhead costs more closely to benefiting activities and resulted in significant changes effective January 1982. These changes increased overhead allocations to service line II substantially. (For example, protection costs were directed toward service line II because of the valuables handled in the fiscal services.) The unit cost increase of 32.5 percent is a direct result of the continuing volume declines and the increased overhead allocations.

In addition, in 1982 the Federal Reserve Banks were called upon to provide fiscal services to additional government agencies as well as increased services to existing customers. The Treasury also requested procedural changes in the savings bond program, federal tax deposit (FTDs) accounting, and some automation changes. The savings bond stock monitoring program, initiated as a result of GAO recommendations, required more frequent reconcilements, at a greater level of detail, of unissued stock held by issuing agents; many Reserve Banks automated their stock monitoring systems. FTD reporting and reconcilement procedures were also changed as were the Fedwire/TFCS programming edits, both requiring additional resources at Reserve Banks.

In 1983, expenses increased by 4.5 percent and employment declined by 0.7 percent. Overall, volume continued to decline by 3.3 percent resulting in a 7.3 percent rise in unit costs. However, Reserve Bank efforts to improve automated systems continued to be a major factor. During 1983, the Treasury began working with the Reserve Banks to develop a Treasury marketable securities book-entry system for individual investor accounts. The Reserve Banks were also in the process of completing automation efforts in the savings bond program as well as servicing the growing needs of government agencies.

In general, from 1979 to 1984, the Reserve Banks steadily reduced staff levels in fiscal services, maintained small to moderate cost growth, automated several fiscal agency functions and successfully responded to rapidly changing workloads and major Treasury program changes.

Fiscal Agent Reimbursement

The Federal Reserve Banks perform fiscal agency services for the U.S. Treasury, government, quasi-government and international agencies. As fiscal agents, the Reserve Banks perform services as directed under specific statutory authorization. Although the Reserve Banks perform a variety of fiscal agent functions, program responsibility and authority remain with the principal.

Reimbursement for fiscal agent services is obtained through statutory requirements or negotiation with the principal. However, principals are responsible for securing adequate funds to fulfill their statutory program responsibilities.

C. Service Line III - Services to Financial Institutions and the Public.

Service line III in the PACS system includes Reserve Bank costs for providing services to depository institutions and the public. In 1984, this service line amounted to 65.7 percent of total Reserve Bank expenses. Commercial check operations is the largest service in this service line (and in the Reserve Banks). In 1984, check costs represented about 48 percent of total service line costs (and about 31 percent of total 1984 expenses). Currency operations are the second largest group of activities and comprised about 18 percent of the costs of service line III in 1984. Other services and their percentage of service line costs in 1984 are: coin (5 percent), electronic funds transfer (13 percent), government checks and postal money orders (2 percent), securities (4 percent), loans to depository institutions (1 percent), non-cash collection (2 percent), public programs (5 percent), and other activities (3 percent).

In 1984, about 65 percent of service line III expenses were devoted to providing priced services (some began in 1981 and 1982). Virtually all operations in commercial checks, securities, and non-cash collection are priced. Selected operations are priced in the currency, coin, and electronic funds transfer areas. Overall, from 1977 to 1984, expenses increased at an average annual rate of 6.2 percent while employment declined by 1,851 or 18.1 percent.

Table 14
Services to Financial Institutions and the Public (Service Line III)
Expenses and Employment (All Reserve Banks)
(dollars in thousands)

	Expenses					Employment	
Year	Cost of Activities	System Projects	Overhead	Total	Percent Change	Employees	Percent Change
1977	$316,326	$ 2,564	$142,477	$461,367		10,246	
1978	327,419	4,513	147,422	479,354	3.9%	9,840	-3.9%
1979	355,428	4,773	144,171	504,371	5.2	9,790	1.1
1980	386,511	9,271	158,903	554,686	10.0	9,614	-1.8
1981	429,757	15,673	166,268	611,698	10.3	9,480	-1.4
1982	448,073	13,850	184,228	646,151	5.6	8,566	-9.6
1983	468,134	20,390	187,394	675,918	4.6	8.424	-1.7
1984	483,768	23,873	193,813	701,453	3.8	8,395	-0.3
Avg. Annual Growth Rate	6.3%	37.6%	4.5%	6.2%		-2.8%	
Constant Dollars	-.6%	28.7%	-2.2%	-.7%			

From 1979 to 1980, volume in all areas grew substantially, employment declined slightly and unit costs increased in most areas. Beginning in 1981 and throughout 1982, the effect of pricing was evident. A 15.1 percent decline in check volume in 1982, in addition to the 5.1 percent decline in 1981, resulted in an increase in unit costs. The Reserve Banks reduced variable resources in response to the decline in volume. Total employment declined 1.4 percent and 9.6 percent in 1981 and in 1982, respectively and in commercial checks alone, employment declined by 833 employees. However, the adjustment to fixed costs took longer. In 1983, expenses increased only 4.6 percent, employment continued to decline (1.7 percent), volume had stabilized and unit costs were again within acceptable levels. In 1984, expenses increased only 3.8 percent and employment continued to decline.

The MCA has added greater discipline to the Federal Reserve's budget process by requiring matching of costs with revenues for priced services. Reserve Banks cannot budget cost increases unless sufficient revenue can be generated to cover those incremental costs. Also, Reserve Banks must reduce costs if volume declines. This provision adds a market discipline test on existing programs as well as on potential new programs. Also, under its earlier mandate to provide services to member banks, the Federal Reserve was mainly dealing with wholesale financial institutions since member banks tended to be larger banks. Now, however, the number of institutions with access to Federal Reserve services has increased from 5,000 to 40,000, thus increasing the costs of operation considerably. In addition, the System has had to eliminate or price for float. This requirement has led to the implementation of many operations to reduce float levels thereby increasing unit costs. Moreover, the MCA has led the System to a reevaluation of services provided: 1) certain districts have dropped the cash transportation service because the private sector can provide it more efficiently; 2) some districts are developing plans to phase out the definitive securities business because it is not cost justified; and 3) in many instances the Banks have enhanced a number of service offerings which have been favorably received by customers.

Under the joint discipline of MCA requirements and the market for banking services, the Reserve Banks have made substantial improvements to the efficiency of the payments mechanism process (despite significant declines in average personnel):

- Acceleration of check collection has shifted check volume of about $2 billion daily from two-day collection to one-day collection.
- Daily average check float has been reduced by $3.3 billion or 73 percent between 1980 and fourth quarter 1983, and has continued to decline in 1984.
- The Fed has expanded on-line electronic access to approximately 4,600 depository institutions.
- A high dollar group sort program has been designed to reduce incentives for remote disbursement by banks.
- Non-cash availability has improved.
- New net settlement arrangements have been developed.

It is apparent that the Federal Reserve's current production and development expenses are well within the market range. By 1984 the market test of pricing required by the Monetary Control Act was being met, and all costs including float and the PSAF were fully recovered. Total expenditures in this area, including priced and nonpriced services, decreased in real terms at an annual rate of 0.7 percent between 1977 and 1984.

In order to retain its position as a viable provider of priced services as the MCA requires, the Federal Reserve must continue to adhere to the market discipline which it has followed for the last several years. By being a market participant, the Reserve Banks must exercise cost restraint in service line III and make staff reductions when required. The Reserve Banks have demonstrated their ability in cost containment as indeed they must in order to continue to act as a provider of payments mechanism services.

D. Service Line IV - Supervision and Regulation.

Service Line IV in the PACS system includes Reserve Bank costs related to the supervision and regulation of depository institutions. Operations are classified into three services: 1) supervision of district financial institutions - includes costs for all on-site examinations and inspections of commercial banks, international banking organizations, bank holding companies, etc.; 2) administration of laws and regulations related to banking contains costs for processing banking organization and holding company applications, processing condition and other statistical reports, and monitoring reserve accounts; and 3) banking and financial market structure studies capture costs associated with research and analysis of the structure of banking markets. Legislative actions and the rapidly changing environment in the financial industry have had a substantial impact on this service line.

As shown in Table 15, total expenses increased $87.9 million or 15.1 percent on an average annual basis from 1977 to 1984. Employment grew by 612 employees. On an average annual basis, employment increased 5.7 percent per year.

Table 15
Supervision and Regulation (Service Line IV)
Expenses and Employment (All Reserve Banks)
(dollars in thousands)

	Expenses					Employment	
Year	Cost of Activities	System Projects	Overhead	Total	Percent Change	Employees	Percent Change
1977	$36,849	$ 101	$15,748	$52,698		1,273	
1978	40,688	107	17,496	58,291	10.6%	1,337	5.0%
1979	45,393	313	22,048	67,754	16.2	1,411	5.5
1980	55,057	3,437	27,574	86,068	27.0	1,589	12.6
1981	66,210	2,009	31,644	99,863	16.0	1,733	9.1
1982	77,091	6,981	35,244	119,316	19.5	1,796	3.6
1983	87,824	7,820	36,204	131,848	10.5	1,862	3.7
1984	95,554	6,653	38,481	140,690	6.7	1,885	1.2
Average Annual Growth Rate	14.6%	81.9%	13.6%	15.1%		5.7%	
Constant Dollars	7.2%	70.2%	6.3%	7.7%			

System project costs rose significantly from 1977 to 1983. In 1980 the credit control program accounted for an increase of $2.7 million, while the 1982 increase reflects a change in cost allocations. In 1980 total expenses rose by $3.9 million and 96 employees were added to monitor the new reserve accounts.

Throughout this period, various legislative actions and regulatory changes had substantial impact on this service line. The Depository Institutions Deregulation and Monetary Control Act of 1980 meant universal reserve requirements, the phasing out of interest rate regulations and increased access to the discount window. As a result, oversight, monitoring, rule-making and enforcement responsibilities grew. The Garn-St Germain Act resulted in an increased number of mergers involving extraordinarily complex legal, financial and competitive issues. The International Banking Act broadened examination responsibilities for supervising U.S. branches and agencies of foreign banks. Ongoing supervision of domestic banks in recent years has involved substantial monitoring and surveillance of credits associated with distressed industries and foreign borrowers. The Community Reinvestment Act meant new responsibility for evaluating lending records of and working with state member banks to ensure that they are meeting the credit needs of their communities. Several other consumer protection laws were enacted, each mandating specific examination procedures.

Also, the workload in the monitoring of reserve accounts has expanded significantly over the last several years due to: (1) the implementation of the Monetary Control Act of 1980, causing a net increase in the number of reserve accounts to be monitored; (2) substantially more institutions requiring closer monitoring and counseling; (3) the increase in the number of problem banks requiring closer monitoring; and (4) the implementation of a new reserve reporting system.

III. Board of Governors' Expenses and Employment

During the 10-year period 1974 to 1984, operating expenses for the Board increased at an average annual rate of 9.4 percent (2.4 percent in constant dollars). Employment increased by 227 employees or 1.6 percent on an average annual basis. However, as indicated by the following figures, the composition of expenses and employment during the last decade changed significantly.

During the period 1974 to 1977, employment at the Board of Governors increased by 112 employees or 8.2 percent and expenses grew by $13.4 million or 44.7 percent. This growth period was a direct result of several legislative initiatives in the area of consumer regulation. For example, the Board established a new division during this period -- the Division of Consumer and Community Affairs -- to respond to legislatively mandated responsibilities. Legislation included the Home Mortgage Disclosure Act, the Equal Credit Opportunity Act and the Fair Credit Billing Act.

From 1977 to 1979 Board employment fell by 26 or 1.8 percent and expenses increased $3 million or 18 percent. No significant legislative requirements were being placed on the Board and, therefore, through productivity improvements, employment actually declined.

From 1979 to 1980, 69 employees were added, an increase of 4.8 percent. This growth can be directly attributed to the impact of the Financial Institutions Regulatory and Interest Rate Control Act which greatly increased the Board's supervision and regulation responsibilities, primarily in the area of bank holding companies.

From 1980 to 1981, the Board undertook a position control program similar to the program in place throughout the federal government, leading to a reduction of 25 employees. However, with the passage of the Monetary Control Act of 1980, the smaller staff gave the Board inadequate resources to carry out its responsibilities under the Act. Therefore, employment increases were necessary both in 1982 and 1983. Employment increased by only 5 from 1983 to 1984.

Figure 8

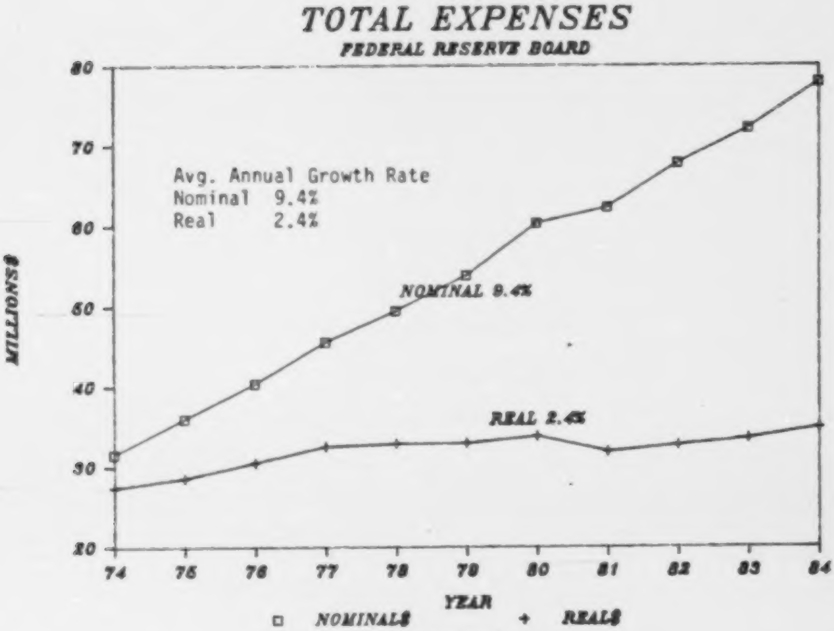
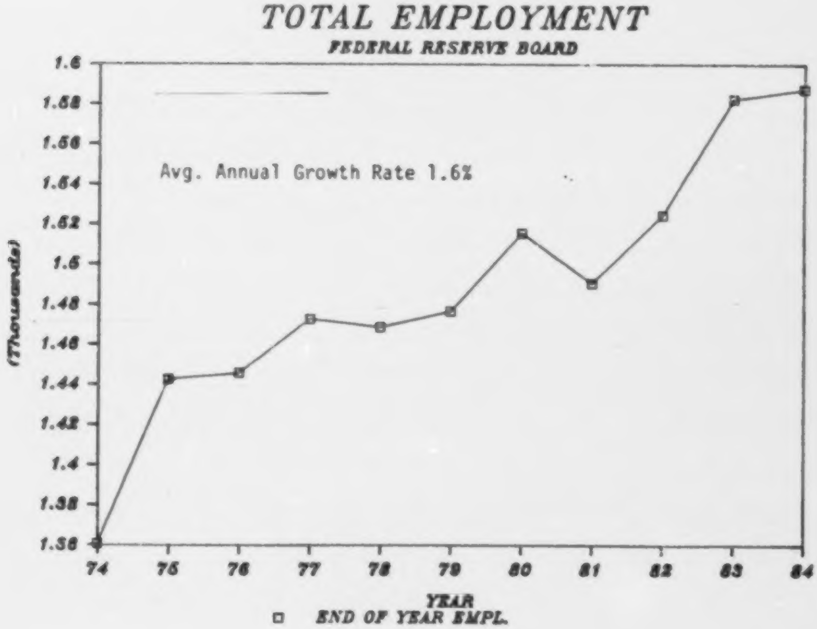


Figure 9



Expenses increased at a greater rate than employment in the last two years due to purchase and lease of automation equipment designed to enhance productivity. In addition, the System's long-range automation program and the MCA required the Board's computers to be upgraded and more staff were added to the Division of Data Processing to support the long-range automation program.

Board Expenses and Employment by Program Structure

Expenses and employment from 1977 to 1984 by the major functional categories of the Board program structure are discussed below. Expenses in the largest category, System Policy Direction and Board Support were $18.5 million and employment totaled 543 in 1977. From 1977 to 1984, expenses grew by a moderate 6.9 percent, or -0.1 percent in constant dollars, while employment grew by 13 or 0.3 percent per year. Expenses in this category fluctuated greatly during the period primarily because of wide swings in the cost of living adjustment for retirees.

Cost containment measures for utilities, mail and facilities support held the increase in controllable expenses to minimal levels during the period and employment actually was lower in 1982 than in 1977. Expenses and employment grew at a faster rate in the last three years of the period because of the data processing costs resulting from the administration information retrieval system, a program designed to integrate administrative data bases, reduce duplication of effort, and lower costs.

The Formulation of Monetary Policy Category is the second largest at the Board. In 1977, expenses totaled $16.3 million with 579 employees. From 1977 to 1984, expenses increased 7.9 percent--or 0.9 percent in constant dollars--on an average annual basis and employment increased 0.3 percent. The expenses and employment levels for this category increased at a very low rate from 1977 through 1979 (8.4 percent and 0.3 percent, respectively). The Credit Restraint Program and Monetary Control Act of 1980 resulted in significant increases from 1979 to 1981. Expenses and employment increased on an average annual basis by 11.4 percent and 3.0 percent, respectively. The increases were primarily associated with new data processing reporting series. Employment actually declined from 1981 to 1984 (-27 or 4 percent) and the rate of increase in expenses declined to 5.3 percent, primarily reflecting the completion of developmental work for data processing projects to support MCA.

The Supervision and Regulation Function has been the fastest growing area at the Board since 1977. Expenses have increased at an average annual rate of 12.3 percent per year from 1977 to 1984, or 5.1 percent in constant dollars, and employment rose by 73 or 4.1 percent on an average annual basis. Consumer legislation in the early years of the period and, more importantly, the Financial Institutions Regulatory and Interest Rate Control Act in 1978 resulted in steady increases in expenses and employment from 1977 through 1980. Problems of financial institutions, and research to keep ahead of changes in the banking industry also led to sharper increases in employment and expenses from 1980 through 1984 than the rest of the Board experienced.

Expenses and employment in the Financial Services to the System, Government and Public Function grew at moderate pace from 1977 through 1982. Expenses increased on an average annual basis by 2.8 percent and employment increased by 7 or 1.3 percent per year. In 1983 and 1984, expenses increased by 20 and 17 percent respectively, in response to requirements to oversee System efforts in pricing. These are expected to moderate considerably. In the 1977-1984 period expenses grew at an average annual rate of 7.0 percent or 0.1 percent in constant dollars.

Table 16
Board Expenses and Employment by Major Function
(dollars in millions)

	Monetary Policy		Supervision & Regulation		Financial Services		System Policy	
	Exp.	Emp.	Exp.	Emp.	Exp.	Emp.	Exp.	Emp.
1977	$16.3	579	$5.8	228	$5.0	109	$18.5	543
1978	17.9	574	7.5	242	4.4	108	19.7	545
1979	19.1	583	8.4	258	4.9	103	21.5	497
1980	21.7	629	9.5	268	5.1	117	23.8	502
1981	23.7	618	10.1	268	5.7	111	23.0	494
1982	25.0	617	11.1	273	5.8	116	26.0	524
1983	26.8	610	11.8	290	6.9	134	26.7	549
1984	27.6	591	13.0	301	8.1	140	29.3	556
Avg. Annual Growth 1977-1978	7.9%	.3%	12.3%	4.1%	7.0%	3.6%	6.9%	.3%
Constant Dollars	0.9%		5.1%		0.1%		-0.1%	

Note: Service lines have been adjusted to include the same services for comparability over time and include estimated capital depreciation.

IV. Description of PACS Performance Measures

Starting in 1978, the Federal Reserve implemented an approach for summarizing its costs per unit of output in individual activities to provide a bottom line for operations. Summary measures are produced both of change in cost of the System and individual districts, and of comparative levels of cost among Districts.

Two main benefits are provided by these summary measures. First, senior management can use them to track and communicate the total results of operations. Second, the summary measures put in perspective cost levels achieved in each individual activity, with small activities receiving relatively little weight and larger activities receiving proportionately greater weight.

General Description

Two types of cost measures are provided--a time-series scale measure and a cross-sectional or inter-District measure. The time series measure compares the expense of producing this year's volume of products with last year's cost levels, and is expressed as a percent change in cost. The cross-sectional measure compares each District's expense with that of producing the District's volume at System-average cost levels.

Relation to PACS

The summary cost measures are constructed from the Federal Reserve's cost accounting system--PACS. They summarize, in dollar and percentage terms, each District's performance. The measures may be used alone, or in conjunction with the detailed cost accounting information which they summarize. Analytical tables are produced which tie the summary measures back into each individual activity and type of expense.

The summary measures include total costs. PACS also provides narrower unit cost concepts such as production costs and productivity measures such as output-per-manhour. These additional measures of cost and productivity may be summarized into aggregate measures.

Productivity

An aggregate unit cost index, composed of more than 20 activities with measurable volume outputs, may be the best overall measure of operating efficiency. This statistic is a weighted index and accordingly is more heavily impacted by developments in the larger operating units, especially commercial check operations, the largest single operation of the Reserve Banks. Due to changes in accounting methods, and in operations themselves, a time span limited to five years is utilized for the time series. Expenses for monetary & economic policy and supervision and regulation are not included in the index because there is no suitable measure of volume output.

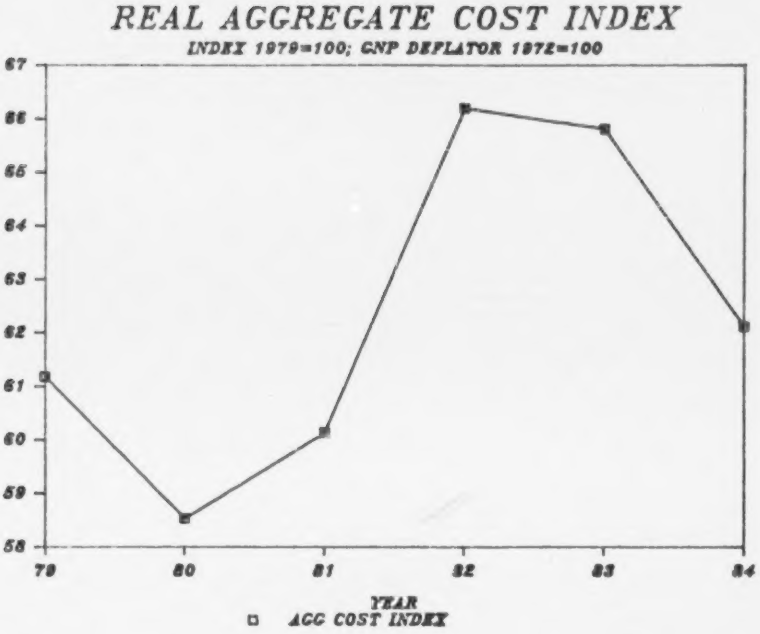
Table 17 shows the pattern of year-to-year changes in the aggregate volume of Reserve Bank operations, as well as aggregate unit costs adjusted for inflation. As Table 17 and Figure 10 indicate, following passage of the MCA and the imposition of pricing, aggregate volumes in the services to financial institutions area declined in 1981 and 1982. While resource adjustments were made, unit costs increased somewhat in 1981 and markedly so in 1982, largely because of the difficulty of reducing fixed costs in the short run. However, over the last two years--partially as a result of increased volumes as well as resource adjustments--unit costs have declined significantly, a pattern that is expected to continue in 1985.

Table 17

Aggregate Unit Cost and Aggregate Volume 1979-1983
(Time Series 1979=100)

	Aggregate Volume		Real Aggregate Unit Cost	
Year	Index	Percent Change	Index	Percent Change
1979	100.00		61.19	
1980	108.41	8.4%	58.53	-4.3%
1981	104.92	-3.2	60.14	2.8
1982	98.07	-6.5	66.91	11.3
1983	102.02	4.0	65.80	-1.7
1984	108.78	6.6	62.12	-5.6

Figure 10


REAL AGGREGATE COST INDEX
INDEX 1979=100; GNP DEFLATOR 1972=100
67
66
65
64
63
62
61
60
59
58
79
80
81
82
83
84
YEAR
□ AGG COST INDEX

IV. The Federal Reserve System's 1985 Budget

In late 1984 the Board of Governors approved 1985 budgets for the Reserve Banks and the Board with total spending of about $1.2 billion. Actual spending in 1984 totaled $1.14 billion. Thus the 1985 budget provides for a maximum increase of about 5 percent (See Table 18). Given expected increases in workload, this 5.1 percent budget increase will require significant cuts in some areas. The budget increase is for all Federal Reserve services, priced and nonpriced, including Reserve Banks and the Board of Governors. After fees for services to depository institutions, expenditures are expected to grow by about 3.6 percent.

System employment is projected to increase by 82, or 0.3 percent in 1985.

Table 18
Federal Reserve System Expenses
1984 Actual - 1985 Budget

	1984	1985	% Change
Monetary & Economic Policy	130.2	131.7	1.1
Services to Treasury & Government Agencies	129.4	140.6	8.6
Services to Financial Institutions	728.2	757.9	4.1
Supervision and Regulation	158.1	174.4	10.3
TOTAL	1145.7	1204.4	5.1

NOTE: These data are for Reserve Banks and Board of Governors expenses excluding currency costs. As discussed previously the data are derived from two separate accounting systems. For comparability over the time periods estimates were made to allocate expenses into major programs and for the Board of Governors which accounts for only 7 percent of the total expenditures.

Table 19
Federal Reserve System Employment
1984 Actual - 1985 Budget

	1984	1985	% Change
Reserve Bank[1]	22,669	22,809	0.6
Board of Governors[2]	1,588	1,530	-3.7
TOTAL	24,257	24,339	0.3

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[1] Average number of personnel.

[2] End of year employment.

This overall increase provides significant variation in budgeted expenditures among functions. For example, spending on monetary and economic policy is expected to increase by about 1.0 percent in 1985. This continues the pattern of reduced spending in this function that started in 1984 after the cost bulges resulting from the Monetary Control Act and contemporaneous reserve requirements had been absorbed. As explained earlier the largest single component of costs in this area is for data collection and preparation.

Expenditures in services to financial institutions and the public are expected to grow by about 4.1 percent. Approximately two-thirds of expenditures in this area are for priced services and are budgeted to rise by 4.4 percent. Just as in 1984, all costs associated with priced services including the cost of float and the PSAF are expected to be recovered.

Expenditures in the nonpriced component of services to financial institutions and the public are budgeted to increase by about 3.4 percent. The principal reasons for this growth in spending are increases in the volume of currency and coin handled by the Reserve Banks and the rise in postal costs.

Spending on services for the U.S. Treasury and other government agencies is budgeted to grow by 8.6 percent. More than two-thirds of this anticipated increase is the result of a new system which will provide computer automated recordkeeping for Treasury notes and bonds held by individuals. This "book entry" approach is already used for Treasury securities held by institutions and for Treasury bills held by individuals. Its extension to Treasury notes and bonds held by individuals is expected to yield substantial savings to the Treasury. This new approach will also provide improved service to individuals buying Treasury notes and bonds and eliminate the need for safekeeping actual paper instruments.

Reserve Banks

The 1985 Reserve Banks' budget allows for an overall increase of $54.5 million, or 5.1 percent, and an employment increase of 141 or 6.2 percent.

Table 20
Reserve Bank Expenses by Service Line[1]
1984 Actual - 1985 Budget

	1984	1985	% Change
Monetary & Economic Policy	99.4	98.4	-1.0
Services to Treasury & Government Agencies	126.3	137.0	8.5
Services to Financial Institutions	701.5	730.3	4.1
Supervision and Regulation	140.7	156.7	11.4
TOTAL	1067.8	1122.3	5.1

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[1] Includes support and overhead allocation.

Table 21
Reserve Bank Employment by Service Line[1]
1984 Actual - 1985 Budget

	1984	1985	% Change
Monetary & Economic Policy	826	833	.8
Services to Treasury & Government Agencies	1,798	1,825	1.5
Services to Financial Institutions	8,395	8,441	.5
Supervision and Regulation	1,885	1,903	1.0
Support	4,340	4,390	1.2
Overhead	5,424	5,417	-0.1
TOTAL	22,668	22,809	0.6

Expenses in the Monetary and Economic Policy service line are budgeted to decline by approximately $1 million or 1.0 percent, and staff is expected to increase by 7 or 0.8% above the 1984 level. The expense decrease is a result of declines in overhead and System project costs, primarily due to completion of the Contemporaneous Reserve Requirement (CRR) System Project. The direct and support expense increases reflect expanded office automation projects in most districts and increased automation efforts for economic modeling and forecasting.

Expenses in Services to the U.S. Treasury and Government Agencies are budgeted to increase by $10.7 million or 8.5 percent over the 1984 level. Staff is expected to increase by 27 or 1.5 percent. Of the expense and employment increases, $5.3 million and approximately 33 personnel are associated with the Treasury Securities Access Book Entry System (T-DAB).

Expenses in Services to Financial Institutions and the Public, both priced and nonpriced, are budgeted to increase $28.8 million or 4.1 percent, and employment is expected to increase by 46, or 0.5 percent. Nonpriced services' expense and employment increases are primarily due to volume increases in both currency and coin, and the impact of open access policy. Priced services expense increases are primarily in commercial check, transfer of account balances, and automated clearing house operations.

Expenses in Supervision and Regulation in 1985 are budgeted to increase $16 million or 11.4 percent over the 1984 level. Employment is expected to increase by 8, or 1.0 percent. The rise in expense will result from an increase in the allocation to Supervision and Regulation of the Integrated Accounting System projects; however, this increase is offset by several Districts' plans to reduce staff.

Board of Governors

Total expenses for the Board of Governors are projected at $3.9 million, or 5 percent increase, over the 1984 level. These figures include a $4.75 million depreciation expense. Employment is expected to decrease by 58, or 3.7 percent.

Table 22
Board of Governors Expenses[1]
1984 Actual - 1985 Budget

	1984	1985	% Change
Monetary & Economic Policy	27.6	29.9	8.3%
Supervision and Regulation	13.0	13.3	2.2%
Financial Services	8.1	8.8	9.3%
System Policy and Board Support	29.3	29.9	1.9%
TOTAL	78.0	81.9	5.0%

[1] Includes depreciation expense. Figures may not add due to rounding.

Table 23
Board of Governors Total Employment
1984 Actual - 1985 Budget

1984	1985	% Change
1,588	1,530	-3.7

Expenses in the Monetary and Economic Policy category at the Board will rise $2.3 million, or 8.3 percent. The largest elements of this increase are associated with the development costs of the resource shared application project (STAT) and the allocation of costs, including depreciation, for the contingency processing center.

Expenses in the Supervision and Regulation category are budgeted to increase by $300,000 or 2.2 percent. Increases in this area are being offset by reductions in the volume of work of the Division of Consumer and Community Affairs and a decrease in the use of data processing resources.

The financial services categories are budgeted to increase by $700,000 or 9.3 percent. The major cause of the increase is the improvement to the planning and control system (PACS), which will facilitate comparison of revenue and expense projections with actual data as they become available.

System Policy and Board Support costs are budgeted to rise by $600,000, or 1.9 percent. The relatively modest size of the increase is associated with reduced nonpersonal costs in 1985 for publications and repairs and alterations for the Board's facilities.

Representative HAMILTON. Thank you very much, Mr. Volcker.

First, let me make very clear that there are a number of things I am not trying to do here with this proposed bill. I do not want, as you recognize in your statement, to jeopardize the independence of the Fed in its conduct of monetary policy. I am not accusing the Fed of wasteful expenditures. I think one of my predecessors in the Congress, Wright Patman, sometimes did that and I suspect he may not be in the Federal Reserve's "Hall of Fame." But that's not my intent.

I was impressed by the tone of your statement. I think in a number of places you indicate a willingness to be receptive to proposed changes in making your budget more understandable and more accessible. And I appreciate that very much and will probably have some suggestions for you as this hearing proceeds.

Now if there is a difference in your approach and mine, I guess it is pointed out in your prepared statement where you think that the proposed inclusion of the Federal Reserve's expenditures with the executive's budget documents could be the first step down a slippery slope. And I can understand your concerns about that, but I do not think that would be the case and, if I did, I wouldn't propose the bill that I do.

You are correct when you state that the Fed releases an awful lot of information about your budgeting proposals, but what strikes us as we try to look at that is that it is very, very difficult to understand and comprehend and that your accounting practices are different from the rest of the Government's, and I suspect that there are not very many Government groups that could not make an argument for some deviation from the standard Government budgeting accounting practices.

But we have to be able to make comparisons and we have to be able to have a budget that has uniform practices in it, and we cannot, it seems to me, permit each Government agency to have a separate accounting system. If we permitted that, then we would have chaos in the Federal budget and it would be absolutely incomprehensible to Members of Congress and also to the American public.

Now your budget information is released on a calendar year basis. The Federal budget, of course, is not. Your budget uses different accounting techniques from the rest of the Government. You mentioned the one on capital expenditures. Also, your budget is not published with the rest of the Federal budget and it does not make projections into the future.

So it becomes very difficult for us to make the judgments that we have to make.

Now we have had some experience in trying to find out what is in your budget and we had, for example, a CBO analyst look into the Fed's annual report and he found it almost unfathomable for someone who is not really familiar with the Fed's budget and accounting system.

There is not, for example, any summary explanation of the tables or what are in the tables, and that analyst had to make repeated calls to technical people at the Fed to have parts of your planning and control system report explained to him. And I suspect that report is just absolutely ununderstandable to any American citizen except a very, very few people who have extraordinary expertise in your financial systems.

Now you publish your data for calendar years. Why don't you use the Federal fiscal year, October 1 to September 30?

Mr. VOLCKER. To the best of my knowledge, we have always used a calendar year basis, probably going back to the mists of time in the Federal Reserve, because that seemed like the normal thing to do for a business-like operation, and probably more natural for the layman than a fiscal year basis.

But I don't think that's a crucial problem, one way or the other.

Representative HAMILTON. Do you have any objection to doing it on a Government fiscal year basis?

Mr. VOLCKER. It seems unnatural to me, I must confess. I'm used to the other way. Corporations and so forth report on a calendar year basis. We have all the expenditures on a quarterly basis, so you could obviously simply shift the reporting period. I think it would create some internal transitional difficulties. We would have to change the time of the budget cycle, presumably, within the Federal Reserve System, but I can't argue that that's an impossible task. We would have to rearrange our internal affairs to conform to that change.

I guess I would have to ask what purpose is served?

Representative HAMILTON. Well, the purpose it serves is to the extent that we can get all Government budgets following the same practice, the information becomes much more readily understandable to us and comparisons are much more easily drawn.

Budget information is always tough to digest, especially for those of us who aren't very handy with statistics, and when you're dealing with different fiscal years it becomes extraordinarily difficult.

Let me just make this observation and then I'll turn to my colleagues for questions. Your concern is that you will get down the slippery slope and we will push you in the Congress toward some invasion or impairment of your independence.

Let me argue that the other way for a moment, if I may. My impression is that the Fed operated for years and years and years, certainly during the early years that I was in the Congress, without any knowledge on the part of the American people of what the Fed did, and frankly, without very much interest in what the Fed did because they had no perception that the Fed had any impact on their daily life.

Now in recent years, partly under your chairmanship but I think probably under the chairmanship of some of your predecessors, the Fed has become a much more visible participant in the conduct of the economic policy of the Government and there are many of us who now think that the Fed may even be the chief actor in economic policy.

But what is happening in the country, it seems to me, is that people are becoming very much aware of the the fact that what that Board of yours does has a very profound impact on their pocketbooks and they are uncomfortable, as I am, with the fact that a group of people, no matter how well intentioned and no matter how skillful, are basically inaccessible to them—not just basically—they are inaccessible. They really are unaccountable to them and they are not an institution which in any sense is representative.

Now, I understand you can make arguments that the Fed ought not to be representative and it ought not to be accessible, but to the extent that you make those arguments, you make arguments against a democratic government itself, but I recognize that you play a special role.

The point of all of this, I guess, is that I think the pressures on the Fed are going to build and that the people in this country are going to become more and more conscious of the enormous economic power that you have, and the pressures might build for some impairment of that independence.

I would urge you to take the steps that I think you, yourself, think may be necessary, if I read your prepared statement correctly, to be much more open in your accounting procedures to the Congress and to the public, so that you head off some of those pressures.

You may or may not want to respond to my ramblings up here, Mr. Volcker, but I would be glad to permit you to do so.

Mr. **Volcker**. Let me respond to several of the points that you've made, Mr. Chairman.

When I went back and looked at our budget, and particularly the information available about our budget, I did not find it in any sense inaccurate; I don't think those tables in the annual report, from my point of view, are hard to understand, but they are not very fully explained and they are very summary statements. We go from the ready availability of those summary statements into other publications that we have that have enormous detail and are, indeed, very difficult to understand. Those statements are basically an outgrowth of our internal management control systems; they were developed for the purpose of helping to manage the Federal Reserve banks and the Federal Reserve System, and they would be very difficult for a layman to comprehend very readily.

I understand we have an explanatory booklet for them and the explanatory booklet is almost as long as the document itself.

So I think we do fall between two stools. We have very straightforward summary statements and we have extremely detailed statements and we haven't got much in between that's readily available to the public that's easily comprehensible. I think we ought to deal with that problem and that is what we are working on; our latest annual report is at least a step in that direction, but I think we can do more.

Now, you make a point—and I well understand it—that what the Federal Reserve does is of more and more interest to the public and to the Congress. I think that, of course, it is of interest in terms of policy, and we do a lot of reporting to the Congress on policy. Any time you want to get us up here we come up here and discuss those questions that I think are of issue to the American people.

I guess maybe we are bound to have different perspectives but I just deny that we are either inaccessible or unaccountable. We do and are called upon to explain ourselves both in the policy sense and potentially in a budgetary sense. We do have all this information available and we will provide it to you in whatever form in the end you think necessary.

Representative HAMILTON. Mr. Volcker, I didn't mean to suggest that you were inaccessible to Members of Congress. I think you are very, very good about testifying.

When I used the word "inaccessible," I used it in the context of your accessibility to the American people. They just don't have any sense that they can approach the Federal Reserve. It's an institution that is hidden behind marble walls and they just can't get at it.

Mr. VOLCKER. A lot of people do approach us. But be that as it may, I think the issue here, in the context of what you have put forward, is what can be most helpful in terms of public understanding and congressional understanding of our budgetary processes, our management, and all the rest. You say, in effect, we should conform our accounts to what other agencies do, and I say—and naturally I believe this is the better view—that we do, using generally accepted accounting principles, present our accounts—maybe not well, in a public relations sense, but we can improve that—in a way that is simpler potentially to understand, more straightforward, more comprehensible, and I think more readily judged by the Congress.

Now whether the Congress has done that or not is another matter, but I do note in my statement that we went through a period of years where the Senate Banking Committee had a hearing once a year just on this subject. In a way, you don't like it, because you've got to go up there and explain yourself and defend yourself, but I thought that was a constructive process, that an organization like ours has to be prepared to defend itself in public and in probing questions; if we're not able to do that, there's something the matter. I think we are able to do that, and I would really recommend that you take that approach.

The one point that I understand bothers you—and we naturally look at it with a somewhat different perspective—is, of course, you can't permit every agency of Government to present its books in a way inconsistent with other agencies. There, I think you just have to appeal to the history and status of the Federal Reserve. This was looked at very carefully by the President's Commission on Budget Concepts in 1976, I believe. They came to the conclusion that, given the particular status and organization of the Federal Reserve—while they recommended a unified budget and everything to be uniform—the Federal Reserve was left in its present status.

I think there are special reasons, as experience throughout the world suggests. Every government that I am aware of treats the central bank, for budgetary purposes and budgetary reporting, in a way more or less comparable to the way we do, they don't try to force it into the general format of a budget. This is a general problem that every government has, and I would simply point out that there's a lot of history and a lot of international experience that I think does justify special treatment for the central bank.

Representative HAMILTON. Congresswoman Fiedler.

Representative FIEDLER. Thank you.

You mentioned before that you don't have any multiyear expenditure forecasts and I was wondering if you could tell us why that's the practice?

Mr. VOLCKER. We do have processes within the Banks and within the System as a whole that look toward the long-term planning approach and that produce indications of trends as part of a control and planning exercise.

We have not attempted to reduce that to precise budgetary forecasts several years ahead and haven't felt that that is particularly useful.

We do the planning, but we don't try to reduce it to a line-item budget several years in advance.

Representative FIEDLER. Would you please tell me how much depreciation you have taken this last fiscal year?

Mr. VOLCKER. How much depreciation?

Representative FIEDLER. Right.

Mr. VOLCKER. $72 million.

Representative FIEDLER. $72 million, but you don't pay taxes, do you?

Mr. VOLCKER. We do not pay taxes—we pay——

Representative FIEDLER. On your depreciation?

Mr. VOLCKER. We pay property taxes only.

Representative FIEDLER. But aside from those property taxes, why do you take depreciation if you don't pay taxes, aside from your overhead expenses?

Mr. VOLCKER. Because we think that's the way to reflect most accurately the current costs of our services. The capital expenditures are lumpy. Let's say we are buying some new reader sorters for the check department. They are expensive pieces of equipment. And suppose we are replacing a whole series of reader sorters in one particular year. That produces a big lump sum expenditure in year one, but those costs are more accurately and fairly reflected over the useful life of that equipment, which may be 5 or 6 years, so we record that in the expense item as a depreciation rather than as a lump sum expenditure in year one to smooth out the costs over the period that that machinery is being used.

Representative FIEDLER. If you didn't take depreciation, where would that money go? It would be added on to your total profit, wouldn't it?

Mr. VOLCKER. It would just be uneven. There would be the same amount of expense over a period of years. If you recorded all that capital expense in year one and you considered it an expense instead of a capital item, your profits would be reduced in that year and increased in subsequent years and it would give you a lumpiness that I think doesn't reflect the economic realities.

Representative FIEDLER. Well, I'm not an accountant——

Mr. VOLCKER. You see, this is particularly important, if I may say, Congresswoman Fielder, because we price many of our services and the law says, "You cover your costs every year," and if we put in that lump sum capital expenditure as a cost, our prices would presumably have to go way up in that year and in the following year they would come down, and it just doesn't make any business or economic sense to conduct a priced service in that manner.

We depreciated the capital before we had priced services, but this makes it almost imperative that we do it.

Representative FIEDLER. It just seems to me that by utilizing depreciation that you are affecting the amount of money that you are taking off as a part of your costs and that, in fact, that depreciated item which normally is used to offset your tax obligation is being used in a different way here.

Mr. VOLCKER. A private business firm that's paying an income tax would find that tax affected by the way it depreciates, but——

Representative FIEDLER. That's right. It affects the bottom line. That's what I'm getting to.

Mr. VOLCKER. But a business firm, if it paid no taxes at all, if we had no corporate income tax, would certainly capitalize capital expenditures and depreciate them over a period of time, because that's the economic reality. You have an artificial system when you don't depreciate capital expenditures.

That's not terribly important in the Government as a whole, and the budget document serves other purposes than simply a reflection of the cost of Government. It's got fiscal policy purposes. But these expenses are relatively small in the Government as a whole. I think they are relatively more important because we have a lot of capital intensive services within the Federal Reserve, but as I mentioned in my statement, I think you will find accountants, including the GAO, who have looked at the kind of thing that we do and who say the preferred method of accounting is to capitalize assets and depreciate them.

We do not pay income taxes, but in these priced services we impute taxes. So even in setting the prices we assume that we pay taxes, and the depreciation calculation even in that sense would affect that calculation.

Representative FIEDLER. Your retirement fund, could you tell me whether it's fully funded or whether there is any unfunded liability?

Mr. VOLCKER. No, it's not only fully funded, but it is in a sense overfunded, so our current pension costs are very low.

Representative FIEDLER. Thank you very much. That's all the questions I have.

Mr. VOLCKER. Our pension system in the Board of Governors in terms of benefits is the same as the civil service system. It's different in the banks.

Representative FIEDLER. Thank you.

Representative HAMILTON. Congressman Scheuer.

Representative SCHEUER. Thank you, Mr. Chairman.

I wish to reiterate the words of our chairman today in congratulating you on the quality of your leadership in the Fed and congratulating you on your "Cool Hand Luke" testimony today. That's a quality you have shown right along the line and it's much appreciated up here.

Mr. VOLCKER. Thank you.

Representative SCHEUER. I am very sympathetic with Lee Hamilton's feeling that all Government agencies should be responsive and accountable to the people, but there are one or two of them, it seems to me, ought to be less accountable.

One of them is the Supreme Court of the United States. And from time to time I have to thank God for its nonaccountability, and I thank God today in contemplating their decision yesterday that they aren't accountable and that they aren't subject to the political pressures of the moment.

And I have the same feeling about the Fed. I don't have the most sophisticated electorate in the world and never have had, although the electorate I have now is the most knowledgeable and sophisticated of the various electorates I have had in 20 years.

Of all the cockeyed, crazy, diverse, heterogenous, pluralistic body of questions that I have ever been asked, I don't think in the last 20 years I have ever been stopped in the subway or a shopping center or a school playground and confronted by an irate housewife about the way the Fed was running its operation. [Laughter.]

I don't think the public is interested in the Fed. They are interested in the economy, but I agree with Lee Hamilton at least, that if you stopped at 42d Street and Broadway and stopped 1,000 people and asked them what was the effect of the Fed on their prices or their jobs or their rate of unemployment, I think one person might give you a reasonable answer and two or three others might stumble, but 997 of them wouldn't have the vaguest clue of what you were talking about.

You are in a very esoteric business and——

Representative HAMILTON. If the gentleman would yield, I imagine those Indiana farmers are a lot more sophisticated than his are.

Representative SCHEUER. I'm sure they are. I concede that.

But I don't worry about the Fed being accountable to the people. They are accountable to Congress and they should be and there's no question about that here.

I do think that the information about what you are doing could be, as you are candid in saying, ought to be and will be and is being improved from the oligonous mass, the glutinous mass that it is now, virtually an inpenetrable glob of matter, to something that we thumb through, understand and absorb.

Now in your prepared statement, you talk about making different arrangements or improved arrangements in your spending and budgetary processes to be presented at times and in a manner more accessible to Congress and congressional oversight. And I take it, by more accessible you don't mean peer access because we don't have any problem with access right now, but more understandable, more comprehensible, more susceptible to analysis by reasonably competent laymen.

Mr. VOLCKER. I think that is correct.

Representative SCHEUER. Who are not skilled in this arcane science of your sophisticated level of money management and financial accounting.

I think we would like to have some examples. When you say: "We take steps and we are taking steps in that direction," tell us what you're doing. I think it's encouraging that your thinking has come so far and that you are actually doing things. Maybe the nub of the matter is not to improve the accountability of the American public on a subject that I don't think they have a great concern about, but improving our ability to cope with the information that you are giving to us and being able to react more promptly and more intelligently through having the information a little bit more intelligible. Give us some of the for instances.

Mr. VOLCKER. Let me give you one for instance. If you look at our annual report for this year, you will find a chapter on our expenditures, put in perspective over a decade with some explanation of it.

In contrast, if you look at last year's report, I think you will see a single page or maybe two pages that basically have a balance sheet and a statement of income and expenses in summary form and almost no explanation.

I was rather surprised when I looked closely at that report, after talking with your chairman some time ago, as to how little explanation we were providing in that particular form. I suspect that that was a process that occurred over the years and nobody was paying much attention to that part of the annual report and it gradually got condensed to the point of very little.

I would appreciate any reactions that you have, if you have a chance to look at that report, as to the type of information presented and where that might be improved.

We present—it goes on for quite a few pages—documents to the public at the time that the budget is before the Board of Governors for approval, typically in December or late November of each year. In looking at that, while there's a lot of material there, I wonder whether that's organized in a way that is most useful, although there is a lot of information that's fairly readily available there.

The more difficult thing—and where we are still looking at it and working at it—is how to take this mass of very detailed information we have, which is extremely useful if you're expert enough—as I say, this is the basic document we use within the Federal Reserve System to see what's going on in various offices and various functions—and summarize that in a way that doesn't have the level of detail that we find necessary for internal control purposes but would enable the public to get a better, broad look at our productivity, how much we are spending, and what the changes in spending are in different services lines in different areas of the country, and that kind of thing.

Somehow we've got to be able, I think, to develop a document in between the very summary statements we have and those very detailed statements.

If we did have oversight hearings, as we once did—it happened to be before the Senate Banking Committee—that, of course, provides a very powerful incentive to develop materials for the purposes of that hearing that are both comprehensible and comprehensive, and it's that achievement of both comprehensibility and comprehensiveness that's not the easiest thing in the world.

Representative SCHEUER. No, it's not. It's intrinsic to your subject matter that the information is essentially strange and baffling to most of us.

Mr. VOLCKER. A lot of our budget is very straightforward budgeting. The great bulk of our expenditures are in producing services that are very tangible. We clear checks. We have a lot of computers to facilitate the transfer of securities and funds around the country. We count money. We pay out money. And these are very straightforward kinds of operations. They account for the great bulk of our expenditures. They can be measured in terms of productivity, employees involved, and all the rest.

Representative SCHEUER. I appreciate those remarks. Let me say one thing more. Somebody around your shop really cares about the looks of this report and how it appeals to the eye. I don't know whether I should give you credit, but somebody——

Mr. VOLCKER. You can't give me credit, but I'm glad to——

Representative SCHEUER. Somebody went to a lot of trouble. This is something I know something about and in terms of the typeset, the charts, the graphs, the columns, the entire presentation, it's very attractively done and it isn't quite as forboding and discouraging and it doesn't have that paralyzing effect as most Government financial documents when you simply pick it up and look at the first page. Whoever designed this annual report really deserves a gold star.

Mr. VOLCKER. I appreciate that comment and I think it's relevant to the point—really the basic point in my statement. I really feel that if you want to focus more public attention and congressional attention on how we spend our money, you're going to be better off with this kind of reporting than if you find it buried in special analyses of a budgetary document that you can hardly lift and which is in a kind of stylized framework of a Federal budgetary approach.

I could tell you from experience, when I used to be an economic analyst and was more familiar with budgeting and budgeting concepts in detail than I am now, when I was a relatively junior economist and I would turn to the budget for an analysis of some Government programs, I thought I was pretty well informed but I couldn't understand them because the budgetary treatment is so arcane that you have to be a professional budget expert—professional expert in Government accounting techniques—and even then it's difficult to understand what they are.

I think our budgeting is the epitome of crystal clarity compared to some of the stuff you find in the budgetary document, because everything has to be forced into the same format even though a particular operation may or may not be very suitable for that format.

Representative SCHEUER. Thank you very much, Mr. Volcker. I enjoyed your testimony.

Representative HAMILTON. Mr. Volcker, you mentioned how your procedures are an open book and you dwell at some length in your prepared statement on this planning and control system, but let me just give you information about that that we learned.

Regarding last year's planning and control system report, the Fed sent out four copies of it outside the system. Two of them went to Treasury. One went to the Food and Nutrition Service, and one went to the Post Office. None went to the Congress.

Now I don't know just why the Food and Nutrition Service needed that, but this document is not being distributed.

Mr. VOLCKER. Well——

Representative HAMILTON. Now hold on just a minute here. The point I guess is that there is nothing I think that the Fed now does, despite your good intentions, which can be viewed as a substitute for publishing your budget as part of the Budget of the United States, because it is the Government's budget that the Congress looks at and if you are publishing these things and sending out three and four copies, that really is not an open book operation, it seems to me.

Now I don't know how you would respond to that, but from our standpoint, I think that if the Congress is really going to get an idea of how you spend your money, then we have to see it as part of the Federal budget.

The other observation I would make is, you said several times this morning that you make a lot of information available and I think you do. I don't want to quarrel with that point.

The information that you now make available does not threaten the independence of the Fed. Why then would the information that we seek in a little different format in our bill threaten the independence of the Fed?

Mr. VOLCKER. To respond to your last comment—I'd like to come back to the earlier one—I think it is not so much the substance of what you are doing read literally, but what will be read into it perhaps by others. I think you understand that there are others who would want to go further than you want to go and actually bring us under, let's say, the appropriations process.

However you view it, my fear is that this would be considered a step in that direction and a foundation for further steps in subsequent years or maybe even for debate in the Congress on the step that you propose. I think it would give aid and comfort to those who want to go in that direction.

Representative HAMILTON. You understand my point? If you don't take that step, then down the road, as the visibility of the Fed increases, you're going to be forced to a more radical step that you will dislike even more.

Mr. VOLCKER. Yes, I understand that point, and I would like to cope with it by making sure that there can be no complaints about our reporting.

As a matter of human nature, if you will, or bureacratic behavior, if we submitted our budget to the OMB, as I think your proposal would imply—not for their review but submit it through their processes to be added to the budget document—I cannot believe that that agency is not at some point going to say, "Well, now, look, we have this material; why don't you make a change here or there," and "I don't know whether or not that particular expenditure is in conformance with our policy or not." And we say, "Well, you're not supposed to have anything to say about our budget." And they say, "Well, we're printing it as part of our budget document. It's going up there as part of the President's budget and we ought to tell you what to do."

Representative HAMILTON. You come to the Congress then and we will be your vigilant defender.

Mr. VOLCKER. I agree you will be. But I've seen a certain amount of that other kind of behavior and I don't think it goes in the direction we want to go in.

Let me comment on the availability, for instance, of this PACS document, and I already say that that's too detailed and not readily accessible. I don't know who we send it out to voluntarily. We send it to the Food and Nutrition Service. That is, I presume, because among other things that document reflects all the expenditures we make for clearing food coupons, and this would be a way that they could review the expenditures we make for that purpose and for which we are reimbursed.

But it is available to the public and we get relatively few requests, as I understand it and as you would expect. The principal——

Representative HAMILTON. Where is it available?

Mr. VOLCKER. I think it's available at our offices here. I don't know whether it's available at any of the banks.

Representative HAMILTON. Just knock on the door and anybody from the public can get it?

Mr. VOLCKER. Yes, I think somebody from the public can walk in and get it, as I understand it. Demand has not been great. It is used, for instance, by other banks who are interested in the costs that we have in providing services that they already provide. It's that kind of a technical document that provides a lot of detail which they can use maybe for checking their own costs, and for seeing how we arrive at the costs that we arrive at in charging for services.

But I would readily say that this is an area where we can make some improvement. We send out 20,000 copies of the annual report and we send that to Congress. That has fallen in the opposite stool of being too summary, so I think the burden is upon us to develop a report—and we would be glad to send it to every Congressman—that is limited enough to be comprehensible but full enough to be meaningful.

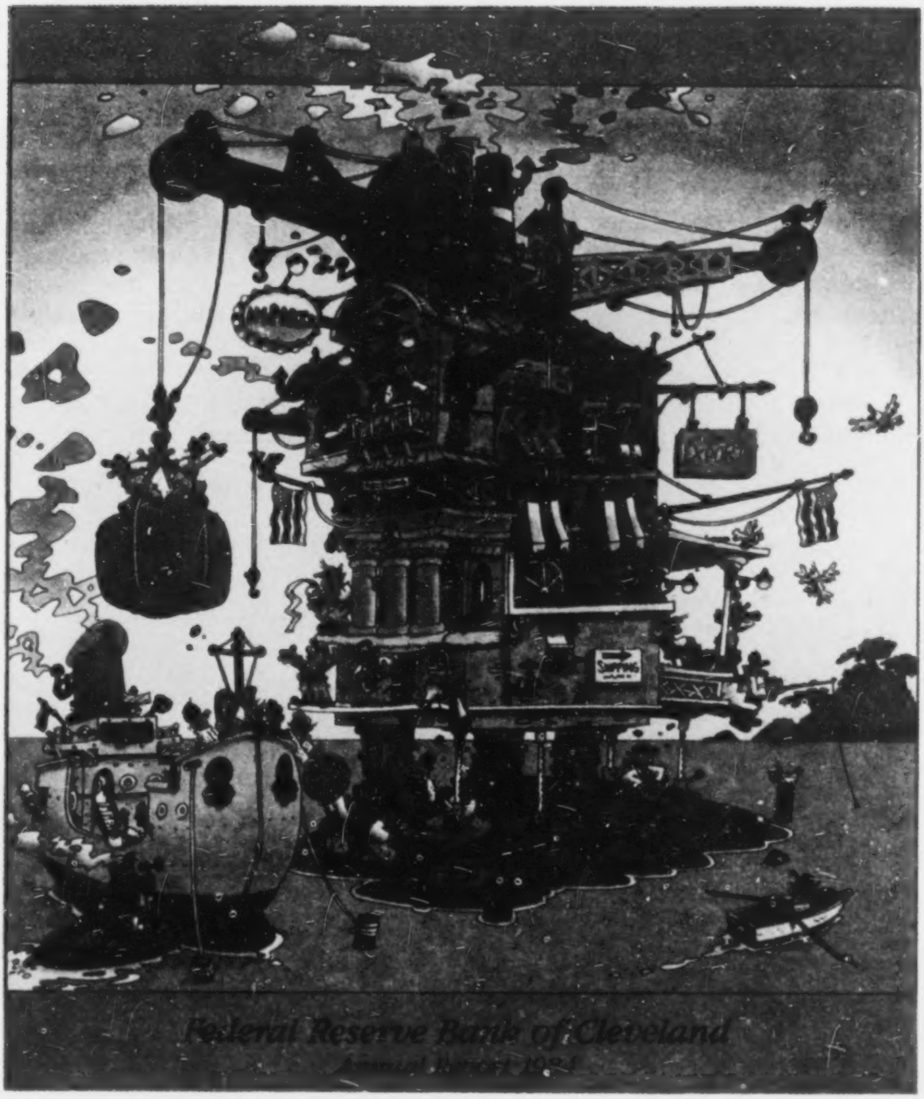
Representative HAMILTON. Mr. Volcker, I don't want to make a major point of this, but I just happen to have on the desk here the Federal Reserve Bank of Cleveland's Annual Report for 1984. Now that's a marvelously put together financial statement——

Mr. VOLCKER. That may go too far, Congressman Hamilton.

Representative HAMILTON. I want to commend your statisticians for their presentation of budget information so it is clear and comprehensible.

The real point is that this is a very attractive publication, but what strikes you about it is, it's got two pages of financial data in it and 28 pages of cartoons and a good statement on the economy in general. But it is not a very informative piece of literature for serious people, I think, who are interested in accountability.

[The annual report referred to follows:]



Federal Reserve Bank of Cleveland

Annual Report 1984

As international markets become more important to the prosperity of the United States, its economic perspective must shift from internal to external, from a closed economy to an open one. Understanding the workings and idiosyncracies of an open economy requires an open and creative mind. How we see the world depends largely on how we interpret and connect events. Our 1984 annual report helps in this process. We appeal to your imagination, through words and illustrations, to help you attain a better understanding of the world in which we live.

Contents

2 The President's Foreword
5 A Puzzle for the World
29 Directors
30 Comparative Financial Statements
32 Officers

The President's Foreword

Economic activity in 1984 was strong and steady and advanced without a significant increase in the rate of inflation. Perhaps the most puzzling aspect of the past year was the simultaneous strength of the dollar in foreign exchange markets and the growing imbalance in the U.S. international transactions. Instead of declining, as the current account deficit approached record levels, the dollar continued to appreciate, buoyed by substantial net inflows of foreign capital. In part, the net inflow of foreign capital to the United States reflects higher interest rates on assets denominated in dollars. The dollar's strength may also reflect a more favorable return to real capital in the United States than in most other developed countries. Beyond these factors, there seems to have been a fundamental improvement in the way in which foreign investors view the future prospects of the dollar. The dollar's persistent strength is an enigma that portends continued current account deficits in the foreseeable future.

The strong dollar has greatly reduced the competitive position of U.S. trade-related industries, and has encouraged protectionist pressures in this country to an extent not witnessed since the Great Depression. The United States was a $24 billion net exporter of goods and services in late 1982 when the current expansion began, but in 1985 the U.S. is a net importer. The traditional capital goods industries bore the brunt of intense foreign competition in the earlier stages of the recovery. Intense competition from imported goods has aggravated the structural problems of the Fourth District's capital goods producers and is now being felt widely throughout the economy.

It is important to note, however, that the effects of the strong dollar have not all been adverse. The dollar's appreciation has reduced import prices, and the resulting intense competition with imports has forced U.S. firms to maintain prices at their lowest possible levels. Moreover, the resulting current account

Two

deficit has, as its counterpart, a current account surplus elsewhere in the world. Our expanding trade deficit has encouraged recovery abroad and has helped the less developed debtor countries to reduce their debt burden.

Concern for the adverse effects of the strong dollar and for the growing current account deficit has prompted policymakers to consider possible options for dealing with the situation. The 1984 Annual Report essay "A Puzzle for the World" examines the issues surrounding the current international situation and reviews the policy choices for correcting current imbalances in U.S. international transactions.

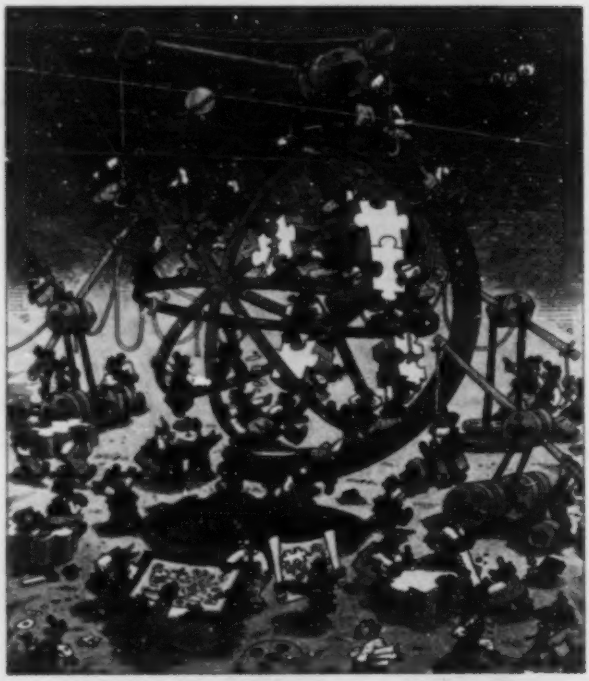
During 1984, the Federal Reserve Bank of Cleveland continued its efforts to provide high quality and efficient services to Fourth District depository institutions. The Bank's activities throughout the year were strengthened by the advice of our 23 directors who represent a variety of banking, business, and educational interests. Richard Fitton (President and Chief Executive Officer of First National Bank of Southwestern Ohio) who served on our Cincinnati Board since 1982, and Robert Milsom (President of Pittsburgh National Bank) who served on our Pittsburgh Board since 1982, completed their terms of service in 1984. John G. McCoy (Chairman of the Executive Committee of Banc One Corporation) completed his term as the Fourth District representative to the Federal Advisory Council. I am grateful to them and to all of our directors for their valuable and dedicated service and guidance. The Bank will also miss the services and enthusiasm of Sister Grace Marie Hiltz, S.C., a Cincinnati Branch Director, who passed away on March 29, 1985. Sister Grace was the President of Sisters of Charity Health Care Systems, Inc.

Finally, I wish to express my appreciation to the officers and staff whose energy, creativity, and commitment made 1984 a successful year.

Sincerely,

Karen N. Horn

Karen N. Horn
President
April 1, 1985



Four

A PUZZLE FOR THE WORLD

The United States is part of a closely integrated, global economic network. International markets have become increasingly important for the U.S. economy since World War II, as the shares of international trade in domestic production and consumption have risen. U.S. exports and imports averaged 8.9 percent and 8.3 percent of total output, respectively, during the 1970s and 5.9 percent and 4.9 percent of total output, respectively, during the 1960s. By 1984, U.S. exports and imports of goods and services, respectively, accounted for 10.0 percent and 11.7 percent of total output. International financial arrangements have become more integrated as foreign trade has expanded and as technological developments have improved communications.

Events of the past few years have clearly illustrated the extent and importance of international interdependence. The growing trade deficit, the strong dollar, the rise in protectionist sentiments, the moderation in U.S. inflation, the net inflow of foreign capital, and the improved international debt situation are all pieces of the same economic puzzle. Each piece is distinct, yet is integrally related to the other pieces, and each is vital for an understanding of the current world economic situation. As with any puzzle, to understand it we must assemble the pieces and try to relate them to each other.

The task is not easy; pieces that appear to fit together often do not. A simple, straightforward relationship between the trade balance and the dollar is a case in point. When we find pieces that do not fit together, we must reexamine the puzzle and reevaluate the relationships.

Perhaps no other puzzle has generated more controversy and misunderstanding than the current international economic situation. This annual report attempts to understand the international economic puzzle by examining recent developments and showing how they are related to each other.

Five

PROBLEMS IN THE CURRENT ACCOUNT

The most disturbing aspect of the recent economic developments is the growing imbalance in U.S. international transactions. Due to the relative strength of the U.S. economic recovery, and to the strong dollar in foreign exchange markets, imports have flooded the U.S. market while U.S. exports have fared poorly. Consequently, U.S. industries that compete against imports, and U.S. export-orientated industries, are not experiencing the rapid pace of economic growth that other sectors have enjoyed. The situation has rekindled protectionist sentiments which now seem stronger than at any time since the Great Depression. While an associated inflow of foreign savings has helped to finance both public and private credit demands, and to keep U.S. interest rates below levels they otherwise would have reached, such savings flows could evaporate quickly, with adverse consequences for domestic interest rates, as the recovery abroad proceeds. This section investigates recent developments in U.S. international transactions, surveys the factors that underlie these transactions, and describes their interrelationships.

INTERNATIONAL ACCOUNTS.

In an accounting sense, international transactions that constitute the balance of payments always balance. This is more than a purely mechanistic balance; underlying it are numerous transactions, public and private, domestic and foreign, that are responding to many economic variables. The transactions create both demands for dollars and supplies of dollars. Any tendency of the transactions not to balance in total will cause adjustments either in exchange rates, or in other economic variables that will insure a balance.

U.S. BALANCE OF PAYMENTS

Current Account
Balance of Goods and Services
Unilateral Transfers

Capital Account
Government
  Official
  Unofficial
Private

Errors and Omissions

When economists speak of disequilibrium, or imbalance, in international accounts, they refer to the *way* in which this ledger balances. Most observers define equilibrium in terms of the current account, which measures international trade in goods and services and unilateral transfers (see box). The current account need not always balance. Temporary factors, such as strikes and business-cycle fluctuations, artificial barriers to international transactions, and exogenous shifts in the terms of trade can result in current-account deficits.[1] Moreover, a surplus or deficit can persist if supported by equally persistent private capital flows, but experience has shown that large imbalances in the current account generally are unsustainable. Large current-account deficits usually produce adjustments in exchange rates, in domestic and foreign income levels, and in prices that eventually restore equilibrium in the account.

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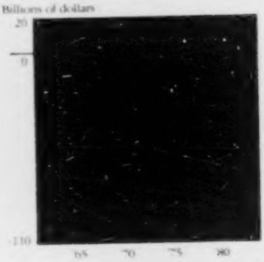
[1] See *"The Exchange Rate System: Lessons of the Past and Options for the Future. A Study by the Research Department of the International Monetary Fund,"* Occasional Paper, No. 30, Washington, DC: *International Monetary Fund, July 1984.*

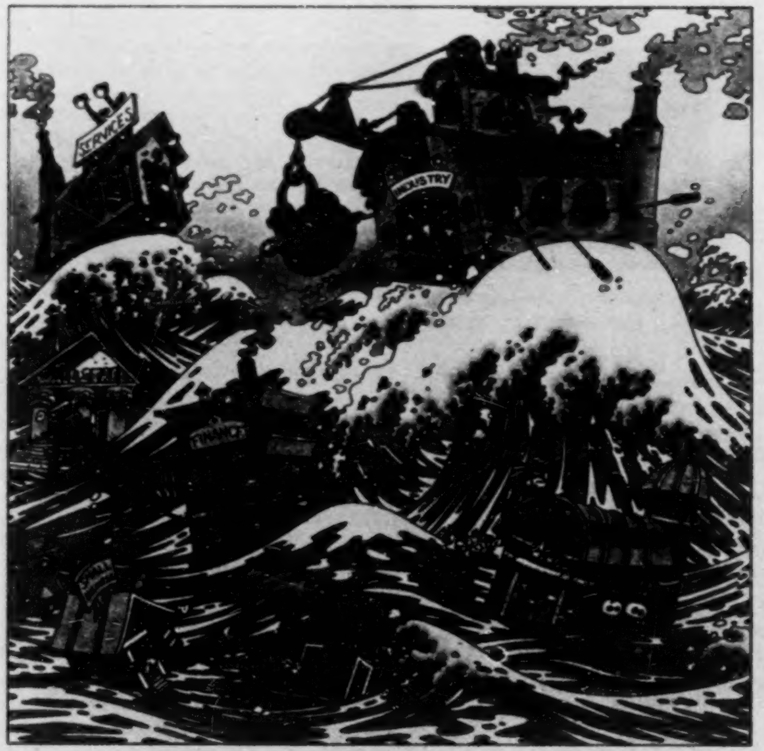
Throughout the post World War II period, the United States typically has run small current account surpluses. These surpluses were large immediately following the war, but rarely exceeded 1 percent of GNP during the 1950s and 1960s. On only three occasions during the 1950s and the 1960s, did the United States run current account deficits, but these deficits were small and did not persist very long. By the 1970s, the United States could no longer regard a surplus in the current account as the most likely state of affairs. We experienced current account deficits in 1971 and 1972 and again from 1977 through 1979 (see figure 1). In 1982, the current account shifted again to a $9.2 billion deficit that widened in 1983 and grew to $101.6 billion in 1984. The deterioration in the U.S. current account since 1982 primarily reflects a rapid widening of the U.S. merchandise trade deficit; however, an unprecedented shift in U.S. services trade from a surplus to a deficit also was a factor. The United States usually posts a deficit in its merchandise trade, but usually offsets this with a larger surplus on its trade in services. Most analysts expect the current account deficit to widen further in 1985 and 1986, although not at the pace experienced last year.

Figure 1
U.S. Current Account Balance



SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis

CURRENT ACCOUNT AND CAPITAL FLOWS. The tendency of the international accounts to balance transcends accounting principles because of the need to pay for imports either with exports or through the exchange of financial claims. If a country, like the United States, is not exporting goods and services in sufficient quantity to pay for its imports, that country either must trade foreigners a claim on its future production, or must reduce its financial claims on its trading partners. Countries running persistent current account deficits experience net inflows of foreign capital, as they sell off existing financial and real assets or create new financial liabilities. Foreigners will acquire more stocks, bonds, bank deposits, real estate, etc., previously held by residents of the deficit country. If their current account deficits persist, even countries that were once net creditors to the rest of the world eventually become debtor nations. Conversely, countries maintaining current account surpluses experience capital outflows as they reduce their liabilities to foreigners and accumulate foreign assets; their net investment position grows. In this manner, a capital inflow (outflow) accompanies a current account deficit (surplus).


SERVICES
INDUSTRY
FINANCE

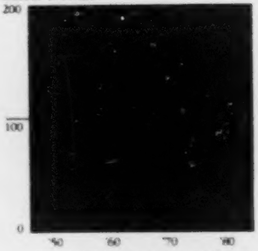
Eight

During the 1950s and 1960s, the United States acquired large amounts of foreign assets by running almost persistent current account surpluses; our net international investment position grew (see figure 2). Recent current account deficits have produced a sharp deterioration in our net international investment position, and the current account deficits projected for 1985 and 1986 indicate that the United States will become a debtor nation sometime this year; that is, total U.S. liabilities to foreigners soon will exceed total U.S.-held foreign assets.

BEHIND THE CURRENT-ACCOUNT DEFICIT. The observed value of any economy's production will equal exactly its income, and will equal exactly the value of its consumption, investment, government spending, and net exports. Any nation that absorbs more resources through consumption, investment and government spending than it produces, necessarily imports more goods and services than it exports. Because such a nation is absorbing goods and services in excess of its nominal income, its domestic savings will be insufficient to finance investment and any government deficit. A deficit country, therefore, also experiences a net inflow of foreign savings.

Although these relationships are always true, the manner in which their components add together provides a clue to factors underlying current-account developments. For the recent U.S. experience, the saving relationship is most instructive. Initially in 1982, as the current account shifted to a deficit, growth in gross private domestic savings slowed, reflecting the recession and a slowing in the inflation rate. Private investment declined in 1982, but the government deficit grew more rapidly than could be accommodated out of private domestic savings even with the decline in investment. After 1982, private domestic savings grew at a faster pace. Although it remained very large, the government deficit grew more slowly in 1983 and declined in 1984. Gross private investment, however, recovered quite sharply, especially in 1984. With large government deficits, the increase in private investment exceeded private domestic savings and attracted a net inflow of foreign capital. Heavy public and private credit demands, therefore, play important roles in explaining recent international transactions. We now must go beyond these general relationships and discuss the developments that underlie the configuration among saving, investment, the government deficit, and the current account.

Figure 2
International Investment Position of the United States



NOTE: The 1984 data point is estimated from preliminary information on capital flows for last year.
SOURCE: U.S. Department of Commerce, Bureau of Economic Analysis.

USUAL RECOVERY PATTERN. A deterioration in the U.S. current account is fairly typical during the early stages of a business recovery. Economic recoveries in the United States usually lead recoveries abroad; in the early stages of an upturn, U.S. imports typically rise faster than U.S. exports. The current recovery, which began late in 1982, was no exception. The U.S. economy grew 6.3 percent in 1983 and 5.9 percent in 1984, while economic recovery among the industrial economies advanced at less than 3 percent in both of these years.[2] The recoveries in the less-developed countries also proceeded more slowly than the recovery in the United States.

As these cyclical developments produced an expanding U.S. current-account deficit in 1982 and through 1983, many exchange-market analysts anticipated a depreciation in the dollar, reasoning that such a depreciation was necessary to eliminate the current-account deficit. The dollar did not depreciate. Instead, the dollar appreciated 11 percent in 1983 and 12 percent in 1984 on a trade-weighted average basis. The dollar's appreciation further aggravated the current-account deficit by lowering the dollar price of U.S. imports and by raising the foreign-currency price of U.S. exports. According to some estimates, slightly more than one third of the deterioration in the current account over the past four years is attributable to the dollar's appreciation over that period.[3]

A FUNDAMENTALLY DIFFERENT DEFICIT. The dollar's appreciation resulted from the heavy demand for dollar-denominated assets that is largely reflected in the substantial net inflows of private foreign capital to the United States. Beyond the cyclical developments taking place in the U.S. economy, structural changes underway both here and abroad precipitated major changes in the historical pattern of world capital flows. These changes include a growing structural budget deficit in the United States, an improved return on real investment in the United States, increased confidence worldwide in U.S. policymakers' resolve to combat inflation, and political concerns in many foreign countries. These factors altered the basic nature of the U.S. current-account deficit.

Net outflows of private capital accompanied the U.S. current-account deficits experienced in 1971 and 1972 and between 1977 and 1979. These outflows of *private* capital reflected a general lack of confidence in the dollar and in U.S. economic policies. The dollar depreciated in foreign exchange markets. At the time, net inflows of *official* capital, reflecting attempts to support the dollar, helped balance the international accounts, avoiding even sharper adjustments in exchange rates, or changes in income levels and in other economic variables.

Since 1983, however, the situation has been reversed. The U.S. current account deficit has been accompanied by net inflows of private capital, amounting to $33 billion in 1983 and swelling to $77 billion in 1984.[3] In general, the net inflow of private capital to the United States seems to reflect changes in the investment patterns of both U.S. and foreign investors. Much of the change appears to reflect a significant shift in bank related capital over the past few years. In the past, the United States usually has experienced a net outflow of bank related capital, but this net outflow narrowed in recent years and shifted to a net inflow in 1984. Last year, in particular, there was also a substantial increase in foreign demand for U.S. Treasury securities and U.S. corporate bonds and a stronger inflow of foreign direct investment to the United States.

Unlike the past, a lack of confidence in the dollar and in the U.S. economy has not accompanied the recent current account deficit. These net inflows of private capital, however, have helped to maintain a strong dollar exchange rate, have enabled the current account deficit to persist, and have caused international economists to rethink theories suggesting a rapid adjustment to current account imbalances.

MOTIVATING FACTORS. Many factors have encouraged a net inflow of foreign capital to the United States. The leading factors are interest rate differentials that favor investment in dollar denominated assets over assets denominated in other currencies, an improved climate for investment in real capital in the United States, and concern over political and social stability elsewhere in the world.

The most often cited factors encouraging capital inflows and keeping the dollar strong in foreign currency markets are interest rate differentials favoring dollar denominated assets over assets denominated in other currencies. Large federal budget deficits, and the prospect that these federal budget deficits will remain large for the remainder of the decade, appear to be important factors contributing to higher U.S. interest rates. The relationship between federal budget deficits and higher interest rates is not simple; it

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2. Growth rates are for the 10 largest foreign countries, expressed on a trade weighted average basis.

3. Statement by Henry C. Wallich, Member of the Board of Governors of the Federal Reserve System, before the Subcommittee on International Economic Policy and Trade, Committee on Foreign Affairs, U.S. House of Representatives, Washington DC: Board of Governors of the Federal Reserve System, March 22, 1985, p. 2.

4. Many economists believe that the errors and omissions entry in the balance of payments data consists, in large part, of unreported private capital transactions. The errors and omissions component has been quite large on balance in recent years and has consistently suggested further private capital inflows since 1978.

greatly depends on how the fiscal policies that generated the deficit influence private investment and savings. For example, a $25 billion deficit produced solely by measures that increase saving $25 billion probably would not affect interest rates.

Most empirical investigations of the relationship between federal budget deficits and interest rates generally have failed to verify that deficits produce high interest rates. This result probably reflects the fact that federal deficits have risen during periods of economic slack when private credit demands are weak, and they have moderated fairly quickly again when recovery was under way and private credit demands firmed. Moreover, federal borrowing historically has remained fairly small, on balance, relative to private saving. As discussed in last year's annual report, federal borrowing has risen sharply relative to private saving since 1979. In addition, private investment spending has been atypically strong over the recent recovery. Interest rates undoubtedly have been higher than they would have been in the absence of the enormous federal credit demands.

Nevertheless, heavy federal borrowing appears to have had less effect on interest rates than analysts had anticipated, and it has not hampered growth of the interest-rate-sensitive sectors of the economy to the extent earlier feared. The massive inflows of foreign savings which have accompanied the current account deficit have helped finance both public and private credit demands. At present there is little prospect for a sharp decline in the federal demand on private savings, as structural deficits probably will remain in a range of 4 to 5 percent of GNP throughout the decade. As the U.S. expansion continues, and as private credit demands continue to firm, heavy federal borrowing seems likely to put further upward pressures on interest rates.

While heavy federal credit demands and a strong U.S. recovery maintained pressure on U.S. interest rates, the slow recovery in Europe resulted in weak credit demands there. In addition, Eurodollar markets remained liquid because foreign exporters have deposited dollars earned through trade with the United States in these markets.[5] The weak recovery abroad and the liquidity in the Eurodollar market helped to produce interest-rate differentials that favored dollar denominated assets and contributed to the inflows of capital to the United States.

An improved investment climate in the United States, in relation to other countries, was another major factor contributing to the net inflow of foreign capital, especially longer-term direct and portfolio investment. The return on real capital in the United States appears to have risen substantially since 1982. The improved return on real capital reflects the vigorous recovery in the United States, achieved without a resurgence of inflation, and changes in tax laws that improved depreciation allowances and investment credits. In addition, the cost of investment goods in particular has declined over the last two years, while other business costs including unit labor costs have risen only moderately.[6]

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[5] See Roger M. Kubarych, "Financing the U.S. Current Account Deficit," Quarterly Review, Federal Reserve Bank of New York, vol. 9, no. 2 (Summer 1984), pp. 24–31.

International investors now appear to hold more sanguine expectations about the future prospects for real growth in the United States, and have a renewed confidence in the willingness, and ability, of U.S. policymakers to prevent a rekindling of inflation. The high and variable rate of inflation experienced throughout most of the 1970s made it difficult for investors to assess the relative returns from individual projects. As a consequence, all too often during the 1970s, firms undertook investments with relatively rapid payback instead of the longer-term investments important for building the capital stock and for improving productivity growth.

In contrast with developments in the United States, the long-term investment climate in most other developed countries, especially those in Europe, does not appear to have improved. The recovery in most other developed countries, except in Japan and in Canada, has been sluggish. The European economies, in particular, face numerous structural problems and disincentives that have dampened employment and investment. These problems and disincentives include high nonwage labor costs, job security arrangements that limit labor mobility and new hiring, high marginal tax rates on labor and capital, and heavy regulatory burdens.[7]

In addition to relative rates of return, international investors consider the risks of investing funds in various currencies and countries. Much of the net inflow of foreign savings to the United States in recent years reflects the flight of capital away from political and economic instability elsewhere in the world. Latin America debtor nations, for example, have experienced severe difficulties in servicing their international loans, and the austerity measures undertaken in some of these countries have generated social strife. Many individuals, fearing increased capital controls and possibly the confiscation of assets, have moved funds out of Latin American countries and into dollar-denominated assets in the United States. The safe haven motive is not peculiar to capital movements from Latin America. Strikes, political unrest, and fears of capital controls also may have motivated capital flows from Europe and from the Middle East.

[6] See Economic Report of the President, *Washington, DC: U.S. Government Printing Office, February 1985, p. 31.*

[7] Economic Report of the President, *Washington, DC: U.S. Government Printing Office, February 1985, p. 109.*

IMPACTS OF OUR DEFICIT. The U.S. current account deficit has important implications for the rest of the world. The mirror image of the U.S. current account deficit is in principle a current account surplus elsewhere in the world; our imports are their exports.[8] When the United States imports more than it exports worldwide, it tends to increase production and employment elsewhere in the world. At the same time, however, the flow of foreign savings into the United States that necessarily accompanies a U.S. current account deficit will tend to raise interest rates abroad and slow investment and interest sensitive spending in these countries. The net impact of the U.S. current account deficit on our trading partners depends on how these two influences balance.

Over the past few years, the recovery among most developed foreign nations has been very sluggish; most continue to experience high rates of unemployment and excess capacity. Public and private credit demands in these nations have been rather weak. In this economic environment, the favorable effects on foreigners generated by U.S. imports probably have outweighed the adverse effects stemming from heavy capital flows out of their countries into the United States.

The implications of the U.S. current account deficits for the less developed debtor nations are of special interest. Although the international debt situation remains a major uncertainty, the crisis atmosphere seems to have dissipated in 1984. The prospects of a major disruption in servicing international debt, with cataclysmic consequences for U.S. banks, seem much smaller now than in 1983 or in 1984. Under the auspices of the International Monetary Fund, many debtor countries experiencing severe loan servicing difficulties have renegotiated the terms of their loans and stretched out repayment schedules. Most nations now are sharing in the economic recovery.

With the immediate situation apparently under control, it is time to examine the problem in a longer term context and to consider the implications of solving the debt situation. A necessary element of that solution is that creditor nations as a group run current account deficits with the debtor nations; otherwise, the debtor nations will be unable to earn the necessary foreign exchange to service their loans.

If the debtor nations are to continue servicing their dollar denominated loans, they must obtain dollars. Countries can earn foreign currency by selling assets, by inviting direct foreign investments into their countries, or by running a surplus in their trade of goods and services. Because most less developed debtor nations have few attractive assets to sell and, at present, offer few attrac

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[8] Although it is true in principle that one nation's current account surplus is a current account deficit elsewhere in the world, measured worldwide trade flows do not balance.

tive long-term investment prospects, they must earn foreign exchange through an export surplus.

The largest debtor nations have improved their current-account positions since 1981[9] Much of the improvement has resulted from austerity measures through which the debtor nations have reduced their imports, but the developing countries cannot reduce their imports below a minimum level necessary to support their economies. The debtor nations must expand production of their export sector, improving productivity so that they can compete even more effectively in the world markets.

Export expansion, however, can only occur if the markets of the world absorb the exports of the debtor countries. Recent studies have suggested that industrial-country growth of approximately 2.5 to 3 percent per year is necessary if the developed countries are to absorb exports from debtor countries in sufficient quantities to enable the debtor countries to reduce their debt burdens[10] Such growth would provide an expanding world market for the exports of these countries.

In this context, the huge, growing current-account deficit of the United States has helped the debtor nations to earn foreign currency. Of the $71 billion increase in the U.S. merchandise trade deficit between 1982 and 1984, $12.8 billion, or 18 percent, represented net imports from Latin American countries. Growth in the world market, however, will not help resolve the international debt situation if developed nations limit access to these markets with such artificial barriers as tariffs, quotas or "voluntary" marketing agreements. For this reason, the rising tide of protectionist measures is especially disturbing.

UNITED STATES AS A DEBTOR NATION. The $102 billion U.S. current-account deficit experienced in 1984 is not likely to narrow substantially in the near term. Consequently, the United States will become a debtor nation sometime in 1985 or in 1986; that is, total liabilities of U.S. residents to foreigners will exceed total foreign assets held by U.S. residents (see figure 2).

Economic theory suggests that high-savings, low-investment countries will run current-account surpluses, exporting savings to the rest of the world; low-savings, high-investment countries will incur current-account deficits, importing savings from the rest of the world. The usual presumption is that advanced countries, like the United States, are high-savings countries with a low mar-

[9] Economic Report of the President, *Washington, DC: U.S. Government Printing Office, February 1985, p. 106.*

[10] *See Michael Dooley, William Helkie, et al., "An Analysis of External Debt Positions of Eight Developing Countries through 1990,"* International Finance Discussion Papers, *No. 227. Washington, DC: Board of Governors of the Federal Reserve System, August 1984; and William R. Cline, "International Debt: From Crisis to Recovery," presented at the annual meeting of the American Economic Association, Dallas, TX, December 28, 1984.*

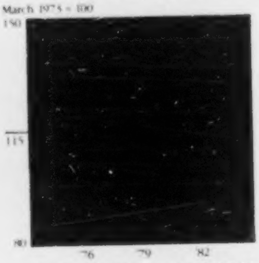
[11] *Shafiqul Islam, "Foreign Debt of the United States and the Dollar,"* Research Paper, *No. 8225, Federal Reserve Bank of New York, September 1984.*

ginal return to investments in real capital because of the relative abundance of capital in these countries. At least through the 1950s and 1960s, the United States seemed to fit this description by typically running a current-account surplus. Nevertheless, developed, capital-rich countries can become capital importers because of a shift in their savings-investment preferences reflecting business cycle developments, secular changes in the return on real capital, or their desire to run structural budget deficits. In the United States, for example, heavy demands for funds to finance the federal budget deficit and private investments currently exceed private domestic savings.[11]

In the short to medium term, the persistence of debtor status depends on the persistence of the underlying factors generating the current-account deficit. In the long run, the ability of a debtor country to expand its debt continually depends on the willingness of foreigners to hold increasing amounts of the debtor's obligations. This willingness has an upward limit related to creditors' subjective evaluations about the ability of the debtor nation to service its debt.

Figure 3
Trade-Weighted Dollar Exchange Rate

March 1973 = 100



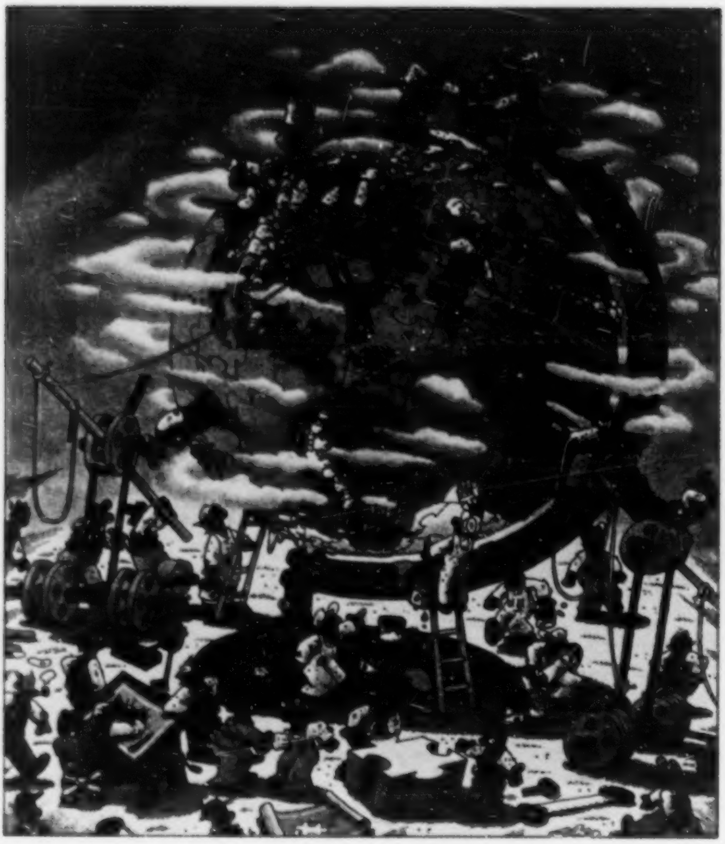
SOURCE: Board of Governors of the Federal Reserve System.

STRONG DOLLAR

The dollar appreciated approximately 72 percent on a trade-weighted basis from mid-1980 through the end of 1984 (see figure 3) and has reached record levels against many currencies, including the U.K. pound and the French franc. Developments of the past few years have demonstrated just how difficult it is to isolate the fundamental economic determinants of exchange rate movements. The dollar's appreciation initially seemed to reflect a change in U.S. monetary policy. Between 1977 and 1979, the trade-weighted dollar depreciated sharply as the U.S. current-account deficit widened, as inflation in the United States accelerated, and as confidence in U.S. policymakers' resolve to end inflation waned. A tighter U.S. monetary policy beginning in late 1979, and an eventual easing in U.S. inflation, appears to have initiated the dollar's appreciation.

Much of the rise in the dollar since 1982, however, has been unanticipated. In early 1983 and again in early 1984, many exchange market analysts expected the dollar to depreciate because of a growing U.S. current-account deficit. Instead, heavy demands for dollar-denominated assets caused the dollar to appreciate approximately 11 percent in 1983 and 12 percent in 1984.

The continued appreciation of the dollar has been a major force shaping the contours of the recent economic recovery. Some of these influences were det



rimental, but others had a positive effect on the recovery. As discussed in the previous section, a major detrimental effect of the strong dollar was the worsening U.S. trade balance, which slowed the recovery in many U.S. industries producing internationally traded goods. Most are manufacturing industries, and many are predominant in the Fourth District.

The adverse consequences of the sharp and persistent rise in the dollar have led to complaints that the dollar is overvalued. "Overvalued" is a difficult judgment to make because it depends on many things. It depends crucially on the economic variables that one believes determine an equilibrium exchange rate, and on the time frame over which these variables operate to correct imbalances. In the short run, the exchange market is almost always in equilibrium, equating supplies of currencies with demands for them. The exchange market consists of many traders, continually assessing information. Because transactions costs are small, and because the market is virtually worldwide, trading occurs almost continuously. In such a market, imbalances will not persist for long.

Individuals who contend that the dollar is overvalued appear to have a different, longer-term notion of equilibrium. Long-term equilibrium implies that the world as a whole is in equilibrium, that is, the markets for goods and services, the markets for labor, and the market for financial assets all are in equilibrium. It furthermore implies that all expectations are met and that all relative prices are constant. The real world, however, is adjusting continually to shocks and to new information. Deviations from this long-term notion of equilibrium are the norm. Consequently, economists who argue that the dollar is overvalued base their judgments about where dollar exchange rates *should* be on a limited set of "proximate causes."

Exchange-market analysts do not completely agree about which factors determine the equilibrium value of exchange rates, about the linkages among these factors, and about the period in which particular factors have their full influence. Usually, however, exchange-market analysts rely on current-account developments, or on international interest-rate differentials when judging the dollar as overvalued or undervalued. When the United States incurred current-account deficits in 1971 and 1972, and again in 1977 through 1979, the dollar eventually depreciated, but, to the dismay of analysts who define equilibrium solely in terms of the current account, the dollar has not responded in a similar manner to the recent, larger current account deficit.[12] Interest-rate differentials also are important determinants of the dollar, but the correlation between interest-rate differentials and the dollar's movements is not always close.

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[12] *Actually, in the absence of the current account deficit, the dollar might have appreciated even more than it has.*

Such "proximate causes" as the current account and interest rates are determined in turn by other factors, including relative rates of real economic growth, relative inflation rates, propensities to save and invest, and technological changes. The relative stance of a nation's monetary and fiscal policies, moreover, influence all of the factors mentioned above and, in that sense, seem the most fundamental of all factors influencing exchange rates.

Exchange rates often deviate from levels predicted by past relationships with these fundamentals because unquantifiable and unpredictable events, such as expectations and noneconomic developments, dominate short-run movements in exchange rates. The unpredictable nature of many daily events affecting exchange markets creates almost random fluctuation in exchange rates. Moreover, markets for foreign currency may react more rapidly to new developments than markets for most goods and services. Consequently, they can overshoot their ultimate equilibrium value when responding to new economic developments. When making decisions to buy or sell foreign exchange, market participants process all available information about past and expected events. From time to time, however, market participants lack complete information about developments in the market, or are slow to form opinions about the implications of new events. In such circumstances, the exchange rate might adjust very slowly, or might move temporarily in the wrong direction.

While the dollar clearly seems overvalued in view of the recent deterioration in the U.S. current account, it is not necessarily overvalued in terms of other factors, such as interest-rate differential, or the high return on real capital in the United States. Even though most economists might expect the dollar to eventually depreciate, they cannot predict when, or how quickly, it will occur.

PRICE PRESSURES AND THE DOLLAR. Not all the effects of the strong dollar were detrimental for the economy. For the first time in over a decade, a significant acceleration of prices did not accompany either the economic recovery or the subsequent expansion. Many factors were responsible for this, including moderate money growth, reduced inflationary expectations, and declines in commodity prices. The rapid appreciation of the dollar, however, was a major factor.

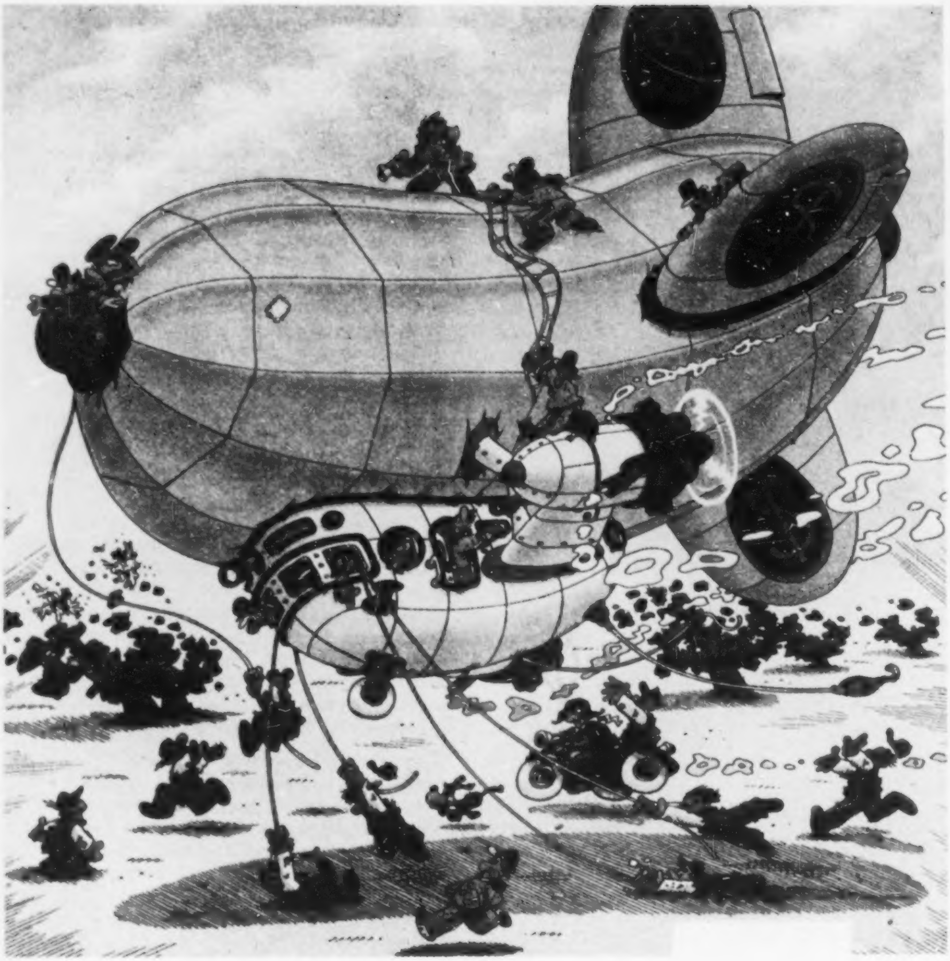
Because the exchange rate is the price of one nation's currency in relation to that of other nations, it is easy to see how exchange rate changes affect the price of one nation's goods and services relative to another's products. It is more difficult, however, to understand how exchange-rate movements translate into aggregate price-level movements within a specific country. The relationship between exchange rates and prices is not simple and direct; nor is it constant over time. Instead, it depends on many factors, including the extent to which resources are unemployed within the relevant country, the size and expected duration of the exchange-rate change, the response of foreign prices to the exchange-rate change, and most important, the stance of monetary policy.

The relationship between exchange rates and inflation is further complicated by a two-way causal relationship that exists between price-level and exchange-rate changes. On the one hand, exchange-rate changes produce price pressures; on the other hand, relative inflation rates among countries are important determinants of exchange rates. To further complicate the relationship, third factors can cause both prices and exchange rates to change, disguising the causal relationship between prices and exchange rates. Ideally, therefore, when assessing the impact of exchange-rate changes on prices, we want to consider exchange-rate movements independent of the inflation process. *Real* exchange rates theoretically record such exchange-rate movements.[13] On a real, trade-weighted basis, the dollar appreciated approximately 65 percent from its low point in 1980 through 1984.

An appreciation in the real exchange rate initially will lower the dollar price of U.S. imports and raise the foreign-currency price of U.S. exports. These initial price pressures will cause foreign and domestic demand to shift away from U.S. goods and services towards foreign goods and services. U.S. firms that compete against imports, or that export goods to world markets, will cut their costs as much as possible and adopt the most efficient production methods to protect their profits and sales against intensified foreign competition. As demand for their goods declines, these trade-related industries will purchase fewer inputs from their suppliers and might reduce their work force. Consequently, prices in the supplier industries and wages could soften. The price pressures will ripple back through the economy to the very basic resources for production, and eventually could affect firms not closely involved with foreign trade.

The extent to which the downward price pressures ripple back through the economy depends on many factors. A small exchange-rate change naturally will have only a small effect on aggregate price levels, whereas a large exchange-rate change will have a larger impact on prices. Even a large exchange-rate change, however, can have no impact on prices if observers expect it to be quickly reversed. Moreover, the effect of an exchange-rate change on domes-

[13] *See Peter Hooper and John Morton, "Summary Measures of the Dollar's Foreign Exchange Value,"* Federal Reserve Bulletin, *vol. 64, no. 10 (October 1979), pp. 783–9.*



tic prices will depend on how foreign prices react to the exchange rate change. If, for example, foreigners react to an increase in demand for their products by raising prices instead of expanding output, they will offset the favorable influence of the dollar's appreciation on U.S. price levels.

The extent to which dollar appreciation moderates U.S. price pressures will depend primarily on monetary policy. The previous example implicitly assumed that monetary policy was unaffected by the dollar's appreciation. If monetary policy became too expansive as domestic prices softened, perhaps to prevent unemployment in trade-related industries, the dollar's appreciation would be blunted, as would the associated price effects. While dollar appreciation can help the disinflation process, it cannot supplant the need for moderate money growth.

Research suggests that on average during the 1970s a 10 percent depreciation of the dollar's real, trade-weighted exchange rate increased consumer prices between 1.5 percent and 1.75 percent, with approximately one-half of the impact occurring within one year of the exchange-rate change, and with the remainder spread over the next two to three years.[14] This rule of thumb suggests that the dollar's recent appreciation trimmed approximately three percentage points off the rise in consumer prices over the 1983–1984 period.

It is difficult to project the dollar's course over 1985 and 1986. Nevertheless, even with a sharp and rapid depreciation of the dollar, this rule of thumb suggests that the impact on aggregate prices would be less than two percentage points because of lags in the relationship between exchange rates and inflation. The exact effect, however, will depend on the relative restraint or ease of monetary policy.

POLICY CHOICES

Many observers, concerned over the detrimental effect of the strong dollar and the huge current-account deficit, have sought action from U.S. policymakers. As discussed in previous sections, U.S. economic policies are important pieces of the international puzzle. Policymakers have many options for influencing various aspects of the international situation. We can summarize these policy options under four broad classifications: 1) expand the money supply at a faster pace to promote dollar depreciation, 2) intervene in foreign-exchange markets to encourage dollar depreciation, 3) institute broad or selective trade barriers to stem the tide of imports into the United States, and 4) trim the federal budget deficit to reduce pressures on U.S. interest rates. Most policy alternatives, however, involve trade offs with domestic economic objectives. Some are ineffective.

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[14] *Peter Hooper and Barbara Lowrey,* "*Impact of the Dollar Depreciation on the U.S. Price Level: An Analytical Survey of Empirical Estimates,*" International Finance Discussion Papers, *No. 128, Washington, DC: Board of Governors of the Federal Reserve System, January 1979.*

By expanding the money supply more rapidly, the Federal Reserve System can promote dollar depreciation. At the current stage of the business cycle, however, rapid money growth would translate quickly into higher prices. As rising prices rekindled inflationary expectations, lenders would raise nominal interest rates to protect the real purchasing power of the funds they lend out. The Federal Reserve could only hope to achieve a permanent reduction in interest rates by continually accelerating money growth. A higher inflation rate would ensue; interest rates would rise; the trade deficit would worsen, but the dollar eventually would depreciate.

Some might argue that recent success at reducing the rate of inflation has provided substantial room for accommodating more inflation in exchange for dollar depreciation. The rate of inflation experienced in 1984, measured by the consumer price index, was the lowest since the late 1960s, and the present outlook for inflation is quite favorable. Nevertheless, the current rate of inflation is still higher than the rate experienced throughout most of the 1960s, and the inflation experience of the 1970s remains fresh in individuals' memories. Inflationary expectations are likely to respond quickly to any evidence that policymakers are not resolved to prevent a resurgence of inflation.

As an alternative to expanding the money supply, some observers argue that the Federal Reserve System could promote dollar depreciation by purchasing foreign exchange with dollars and by offsetting the resulting expansion of the money supply through domestic open market operations. Such a transaction is referred to as ***sterilized intervention***. Sterilized exchange-market intervention seems to offer an attractive alternative to expansionary monetary policy because it would not result in a higher inflation rate.

Unfortunately, the ability of the Federal Reserve System to promote dollar depreciation through sterilized intervention is severely limited. From time to time, when the exchange market is temporarily unsettled, sterilized intervention can reduce exchange-rate volatility. But sterilized intervention cannot produce a lasting dollar depreciation when more fundamental factors, such as interest-rate differentials or relative inflation rates, indicate that the dollar should remain strong. For this reason, the United States decided in March 1981 to cease intervention on a routine basis and to reserve intervention for periods of market disorder.[15]

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[15] *Phillippe Jurgensen, chairman,* Report of the Working Group on Exchange Market Intervention, *Washington, DC, March 1983, and Owen Humpage, "Dollar Intervention and the Deutschemark Dollar Exchange Rate: A Daily Time Series Model,"* Working Paper 8404, *Federal Reserve Bank of Cleveland, September 1984.*

Increasingly, U.S. industries facing intense competition from foreign imports are seeking relief through legislated trade restrictions. Usually trade barriers are industry specific, and occasionally they are aimed at an individual trading partner. Recently, however, some policymakers are considering an across-the-board tax on imports as a method for lowering the U.S. current-account deficit and for providing revenues to trim the federal budget deficit. A comprehensive tariff could help remedy these twin economic problems, but at a substantial cost to U.S. consumers and exporters. Moreover, the tariff could invite foreign retaliation.

Economists have long recognized the benefits of free international trade. When nations specialize in the manufacture of goods that can be produced relatively inexpensively, and when each nation exchanges its goods for the goods of other nations, all nations benefit. The benefits are manifested in lower prices and in a wider set of items available for consumption. Tariffs tend to restrict imports and to raise prices. They transfer income away from consumers toward domestic producers of the protected goods and toward the government. Moreover, tariffs inflict net losses on both national and world economies, because they shift production to less efficient producers and lower the overall level of consumption. Usually the costs of tariffs far exceed their benefits.[16]

U.S. tariffs, or other types of trade restraint, tend to cause the dollar to appreciate under a floating exchange-rate system. By restricting imports, a tariff reduces the supply of dollars in the foreign exchange market and simultaneously lowers U.S. demand for foreign currencies necessary to buy foreign goods. The dollar, consequently, will tend to appreciate relative to the currencies of our trading partners, blunting the impact of the tariff on our imports, and making our exports less competitive in world markets. Consequently, floating exchange rates limit the effectiveness of comprehensive tariffs for improving the current account.

Tariffs and other trade restraints place much of the burden of adjustment on our major trading partners, many of whom derive a major share of their export revenue from trade with the United States, and many of whom import large amounts of goods produced in this country. These countries could retaliate against U.S. trade barriers by restricting U.S. exports to their markets. A tariff, therefore, would harm U.S. export industries because it would inspire either a dollar appreciation, retaliation, or both. With the resulting reduction in exports, the improvements in the U.S. current account would be smaller.

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[16] *See Michael F. Bryan and Owen F. Humpage, "Voluntary Export Restraints: The Cost of Building Walls,"* Economic Review, *Federal Reserve Bank of Cleveland, Summer 1984; Michael F. Bryan and Owen F. Humpage, "Would Taxing Imports Help?"* Economic Commentary, *Federal Reserve Bank of Cleveland, March 1, 1985; and Gerald H. Anderson and Owen F. Humpage, "A Basic Analysis of the New Protectionism,"* Economic Review, *Federal Reserve Bank of Cleveland, Winter 1981–82.*

Given the inefficiencies and the wide range of possible adverse side effects associated with an across-the-board tariff, such a policy seems very costly. Moreover, an across-the-board tariff primarily would address the symptoms of the international problems and not the root causes. As discussed in the previous sections, the large current account deficit in the United States reflects a tendency to absorb resources in excess of our income growth, and to finance such activities through an inflow of foreign savings. An across-the-board tariff does nothing to reduce the rate at which the country is absorbing resources, or to increase permanently the rate of real income growth. By shifting consumption from foreign goods to domestic goods, a tariff will result in higher prices as the economy approaches full employment. This will also adversely affect the export sector and diminish any favorable effects of the tariff on the current account.

Reducing the federal budget deficit is a fourth option open to U.S. policymakers. The first section of this annual report argued that the federal budget deficit is absorbing savings and keeping U.S. interest rates higher than otherwise would be the case. The relatively high level of U.S. interest rates has attracted foreign capital and kept the dollar strong in foreign-exchange markets. Moreover, the pressures exerted from our deficit on U.S. and world interest rates are likely to intensify as recoveries abroad mature, and as industries worldwide reach capacity limitations. A reduction in the U.S. federal budget deficit could help lower U.S. interest rates and could promote a dollar depreciation.

While large federal budget deficits certainly are not the only factor contributing to the dollar's strength, reducing the deficit is the best policy option available. It is the only feasible policy that would not involve costly trade-offs in terms of domestic policy objectives, or that would not result in substantial costs in terms of economic efficiency.

Nevertheless, other factors, such as the high return on real capital in the United States and capital flight into the United States, are keeping the dollar strong in foreign-exchange markets. Therefore, the observed impact on the exchange rate of reducing the federal budget deficit might be small. The dollar's recent strength might be consistent with other economic fundamentals, despite the large current account deficit, and policymakers might be able to alter the exchange rate only if they are willing to alter such things as the return to real capital or the inflation rate. Seldom does cutting the pieces to make them fit solve the puzzle.

Federal Reserve Bank of Cleveland Directors

As of March 1, 1985

Cleveland

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Federal Reserve Agent
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President and
Chief Executive Officer
Cyclops Corporation
Pittsburgh, Pennsylvania

Deputy Chairman
E. MANDELL DE WINDT
Chairman of the Board
Eaton Corporation
Cleveland, Ohio

J. DAVID BARNES
Chairman and
Chief Executive Officer
Mellon Bank
Pittsburgh, Pennsylvania

RAYMOND D. CAMPBELL
Chairman, President, and
Chief Executive Officer
Independent State Bank of Ohio
Columbus, Ohio

JOHN R. HALL
Chairman of the Board and
Chief Executive Officer
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Ashland, Kentucky

RICHARD D. HANNAN
Chairman of the Board
and President
Mercury Instruments, Inc.
Cincinnati, Ohio

JOHN W. KESSLER
President
John W. Kessler Company
Columbus, Ohio

LEWIS R. SMOOT, SR.
President and
Chief Executive Officer
The Sherman R. Smoot Company
Columbus, Ohio

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Mount Vernon, Ohio

Cincinnati

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Chief Executive Officer
Armco Inc.
Middletown, Ohio

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Chief Executive Officer
The Fifth Third Bank
Cincinnati, Ohio

SHERRILL CLELAND
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Marietta College
Marietta, Ohio

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Executive Vice President and
Chief Executive Officer
Harlan National Bank
Harlan, Kentucky

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Health Care Systems, Inc.
Cincinnati, Ohio

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and President
Citizens Federal Savings
& Loan Association
Dayton, Ohio

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Owner, Dunroath Farm
Lexington, Kentucky

Member
Federal Advisory Council
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Chairman and
Chief Executive Officer
National City Corporation
Cleveland, Ohio

Pittsburgh

Chairman
MILTON G. HULME, JR.
President and
Chief Executive Officer
Mine Safety Appliances Company
Pittsburgh, Pennsylvania

CHARLES L. FUELLGRAF, JR.
Chief Executive Officer
Fuellgraf Electric Company
Butler, Pennsylvania

A. DEAN HEASLEY
President and
Chief Executive Officer
Century National Bank
& Trust Company
Rochester, Pennsylvania

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Industrial Administration
Graduate School of
Industrial Administration
Carnegie-Mellon University
Pittsburgh, Pennsylvania

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Vice Chairman
Aluminum Company of America
Pittsburgh, Pennsylvania

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President and
Chief Executive Officer
Gallatin National Bank
Uniontown, Pennsylvania

MILTON A. WASHINGTON
President and
Chief Executive Officer
Allegheny Housing
Rehabilitation Corporation
Pittsburgh, Pennsylvania

Comparative Financial Statement

For years ended December 31

Statement of Condition

	1984	*1983*
Assets		
Gold certificate account	$ 617,000,000	$ 659,000,000
Special drawing rights certificate account	302,000,000	302,000,000
Coin	34,730,126	36,861,081
Loans and securities		
Loans to depository institutions	1,202,000	28,550,000
Federal agency obligations bought outright	464,506,387	512,195,486
U.S. government securities:		
Bills	3,933,137,910	3,899,095,369
Notes	3,612,081,955	3,787,905,782
Bonds	1,270,765,897	1,233,156,486
Total U.S. government securities	8,815,985,762	8,920,157,637
Total loans and securities	9,281,694,149	9,460,903,123
Cash items in process of collection	193,118,962	315,757,611
Bank premises	27,639,546	27,423,020
Other assets	422,751,603	471,760,022
Interdistrict settlement account	707,143,437	(693,739,261)
TOTAL ASSETS	$11,586,077,823	$10,577,965,596
Liabilities		
Federal Reserve notes	$10,124,974,843	$ 8,831,155,014
Deposits		
Depository institutions	882,847,789	1,094,302,278
Foreign	10,350,000	10,950,000
Other deposits	673,094	21,855,551
Total deposits	917,312,347	1,127,107,829
Deferred availability cash items	189,147,400	275,111,613
Other liabilities	146,723,933	141,856,440
TOTAL LIABILITIES	$11,378,158,523	$10,375,230,896
Capital accounts		
Capital paid in	$ 103,959,650	$ 101,367,350
Surplus	103,959,650	101,367,350
TOTAL CAPITAL ACCOUNTS	$ 207,919,300	$ 202,734,700
TOTAL LIABILITIES AND CAPITAL ACCOUNTS	$11,586,077,823	$10,577,965,596

Income and Expenses

	1984	*1983*
Current income		
Interest on loans	$ 2,863,929	$ 2,378,047
Interest on government securities	939,311,393	924,706,072
Earnings on foreign currency	15,021,379	19,987,049
Income from services	34,310,795	30,342,356
All other income	459,292	286,732
Total current income	$991,966,788	$977,700,256
Current operating expenses	55,450,346	54,278,653
Cost of earnings credits	9,195,430	6,514,992
CURRENT NET INCOME	$927,321,012	$916,906,611
Profit and loss		
Additions to current net income		
Profit on sales of government securities	$ 2,779,521	$ 1,336,302
All other additions	3,801	14,243
Total additions	$ 2,783,322	$ 1,350,545
Deductions from current net income		
Loss on foreign exchange transactions	$ 31,382,265	$ 33,309,709
All other deductions	395,929	45,472
Total deductions	$ 31,778,194	$ 33,355,181
Net additions or deductions	($ 28,994,872)	($ 32,004,636)
Assessments by Board of Governors		
Board of Governors expenditures	$ 5,637,400	$ 5,187,600
Federal Reserve currency costs	9,137,397	8,472,971
Total assessments by Board of Governors	$ 14,774,797	$ 13,660,571
NET INCOME AVAILABLE FOR DISTRIBUTION	$883,551,343	$871,241,404
Distribution of net income		
Dividends paid	$ 6,177,578	$ 6,018,002
Payments to U.S. Treasury (interest on Federal Reserve notes)	874,781,466	863,002,352
Transferred to surplus	2,592,300	2,221,050
Total distributed	$883,551,343	$871,241,404

Federal Reserve Bank of Cleveland Officers

As of March 1, 1985

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President

WILLIAM H. HENDRICKS
First Vice President

LEE S. ADAMS
Senior Vice President
& General Counsel

RANDOLPH G. COLEMAN
Senior Vice President

JOHN M. DAVIS
Senior Vice President
& Economist

THOMAS E. ORMISTON, JR.
Senior Vice President

DONALD G. VINCEL
Senior Vice President

ANDREW J. BAZAR
Vice President

DONALD G. BENJAMIN
Vice President

PATRICK V. COST
Vice President
& General Auditor

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Vice President

JOHN W. KOPNICK
Vice President

EDWARD E. RICHARDSON
Vice President

JOHN J. RITCHEY
Vice President &
Associate General Counsel

LESTER M. SELBY
Vice President
& Secretary

SAMUEL D. SMITH
Vice President

ROBERT F. WARE
Vice President

JOHN J. WIXTED, JR.
Vice President

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Assistant Vice President

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Assistant Vice President
& Assistant Secretary

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Assistant General Counsel

LAWRENCE CUY
Assistant Vice President

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& Economist

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Assistant Vice President

Columbus Office
CHARLES F. WILLIAMS
Vice President

Mr. **Volcker**. I would agree with you on this aspect of our operations. These particular reports are developed entirely by the individual Reserve banks, but they can be encouraged to provide more financial information about their own operations, too, and I think some of them do.

Representative **Hamilton**. The Fed is a very, very big operation. You handle a lot of money. You've got a lot of employees over there. You've got 24,000 employees. You're a lot bigger than most departments of Government. You handle a lot more money than most departments of Government, and you're certainly one of the major actors in the American governmental system today so far as your impact upon the lives of ordinary people is concerned.

Well, I think we've had a good discussion here. Do we have any more questions from my colleagues here?

[No response.]

Representative **Hamilton**. I really do appreciate your forthcoming manner in your statement. We're going to take you up, I think, on some of your proposals to talk further with your people about ways to improve information to the Congress and I thank you for your appearance this morning, Mr. Volcker.

Mr. **Volcker**. I appreciate being here and getting some of these issues aired. I do think we need some advice as to how to package the material in the most effective way, which we do not believe is part of the budget package document.

Representative **Hamilton**. Thank you, sir. The subcommittee stands adjourned.

[Whereupon, at 11:05 a.m., the subcommittee adjourned, subject to the call of the Chair.]

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